The Canadian Chartered Accountant

OFFICIAL ORGAN OF

THE DOMINION ASSOCIATION OF CHARTERED ACCOUNTANTS

Published monthly; subscription $3.00 per annum in advance. Advertising rates sent on request.

The Editorial Committee will be pleased to receive contributions on subjects of interest. Papers which may not be deemed suitable will be returned, if desired.

AUSTIN H. CARR, Editor,
10 Adelaide Street East, Toronto

VOLUME XXXVII, No. 4 OCTOBER, 1940 ISSUE No. 207

(The opinions expressed in articles in The Canadian Chartered Accountant are the opinions of the writers of the articles and are not necessarily endorsed by the Association.)

Editorial Comment

The Annual Meeting

A convention of members each year has advantages in that it provides a clearing house for opinions, a means for reviewing the progress of the previous year and an opportunity of discussing plans for the future. In an organization such as the Dominion Association the administration of affairs between annual meetings must of necessity rest with the executive committee of the Council. The review of the year's work in the President's address given at the thirty-eighth annual meeting of the Association held in Montreal last month and published in this issue bears evidence that that duty was discharged in a noteworthy manner by the committee. The consensus of opinion of the annual meeting was that the progress of the profession in the past year exceeded that experienced in any previous year of the Association. The profession owes a debt of gratitude to President Kenneth W. Dalglish and his associates on the executive committee for their untiring efforts in the interests of the profession and of the public; as President, Mr. Dalglish filled that high post with rare ability, and presided at the meetings with such dignity and distinction as to win the admiration of all.

The reading of the President's address cannot but im-

press one with the new responsibilities that the present war has brought to the members of our profession. Perhaps in no single field is the help of the chartered accountant so greatly needed by the government as in the realm of taxation. For the successful prosecution of the war, revenue and still more revenue is needed. The public have come to regard the raising of money by the government as necessary and the increasing of tax rates and imposts as inevitable, and they are prepared to contribute to Canada's war effort through new levies.

All taxing bodies realize that tax measures cannot be prepared hastily. The effect on business and industrial progress of new imposts must be weighed, and the provisions for the successful administration of the tax statutes must also receive very careful study. By his constant contact with the problems of business and his ability to take a detached view where interests appear to conflict, the chartered accountant can study proposed tax measures with an eye to the just interests of the government and the taxpayer alike. The annual meeting expressed its satisfaction that the executive committee was able to make some contribution to the Dominion government when the amendments of the *Income War Tax Act* were under consideration and the provisions of *The Excess Profits Tax Act* revised.

Overlapping in Government Services

This sense of balance inherent in practising accountants and their ability to view the position of the taxing authority and of the taxpayer with a dispassionate eye prompt us, in the interest of national economy, to make reference to an overlapping of government services in some respects which, with the appointment by the government of assistants in many directions during these abnormal times, may dissipate valuable staff material that might well be used to greater advantage by the government or by industrial bodies in other capacities. The weakness to which we draw attention is not peculiar to Canada but creeps into the administrative system of governments everywhere. This situation arises through the genuine desire of administrative heads to assure themselves through their own staffs that the objects of their own particular department are being attained when,

as a matter of fact, that assurance and satisfaction can be had just as well in another way without such an outlay of time on the part of the government. Instead of employing, for instance, numerous government auditors throughout the country investigating the accounts of corporations and other bodies, why, it is asked, does the government not avail itself of the corporations' own auditors?

Use of Firm's Own Auditors

We were interested in reading a reference last month in *The Accountant* (London) to a discussion on this very matter in the British House of Commons. The government there is alive to the possibilities we suggest, and we in Canada can as usual learn much from the people of the Old Land. The Minister of Supply was asked whether he was aware that inconvenience and dislocation of work had been caused by the visits of accountants from more than one department of the government to the same firm and whether steps would be taken to avoid this overlapping in future. The Minister replied that he was fully aware of the danger of overlapping by the accountants of purchasing departments who were concerned with the costs of the same firms. On becoming aware of the situation he had, he said, caused steps to be taken to eliminate duplication of visits by accountants in future and had arranged that the department principally concerned with a firm's costs would investigate them for other departments of the government. Of possibly greatest importance was his next statement: "I may add that it is hoped to diminish the necessity for visits by departmental accountants to investigate firms' costs by utilizing the services of the firms' own auditors. This measure, however, is at present in the experimental stage, but if it proves satisfactory it will be extended. The use of the firms' own auditors will not, of course, affect the department's right to make their own investigation subsequently, should this be considered necessary, but it is hoped that the report of the firms' auditors will in the great majority of cases be sufficient without further check."

Article on Provincial Taxation

What constitutes the paid-up capital of a corporation for tax purposes? What bearing has the figure for goodwill on the determination of

paid-up capital? How are the earned profits of real estate companies determined? These and many other questions are discussed in a series of two articles on taxation prepared for publication by Philip T. Clark, C.A., assistant controller of revenue for the Province of Ontario.

The determination of the tax payable by corporations under today's complicated system of doing business is no ordinary problem. It is one that can be dealt with only by those having an expert knowledge of accounting. The editorial committee is pleased to be able to bring to readers this month the first of these helpful articles; the second will be published in the November issue. In clear and simple language Mr. Clark has dealt with a difficult subject and, while his observations are based on the tax act of Ontario, readers in other provinces will find his references largely applicable in their own jurisdictions inasmuch as the broad bases of taxation throughout the Dominion are similar. Although income tax laws have been on our statute books for years, government officials have shown a diffidence in discussing taxing statutes, not realizing that any enlightenment of the public on the complications of a tax act would go far to ease their own burden of administering its provisions. Mr. Clark has set an example that can with profit be followed by other officials in Canada. These officials are assured by our editorial committee that the pages of this national accounting publication are ever ready to serve them for this purpose.

This Dear Land —This Britain!

War in all its frightfulness is pouring down pain and death and horror these days upon thousands of men and women and children in the stately old capital of our Empire. The feelings aroused in the hearts of Canadians and millions of others throughout the civilized world over such inhuman treatment is too deep for words. Here are harmless mortals, the destruction of whom brings to the enemy no attainment of any military objective. The excuse of a ruthless foe for this wanton act can only be that the inhabitants of the cities and towns of Britain are the soul and body of a nation cherishing the fruits of peace and forming part of a great commonwealth of free peoples bent on seeing that freedom, justice and national pride

shall be the portion of all other nations of the world regardless of race, creed or colour.

The other day we came across a little pamphlet published in Great Britain which if read and digested in Germany and Italy would be an effective reply to the false propaganda spread there against the British Empire. Hitler and Mussolini are trying to persuade themselves and everybody listening to their diatribes that the people of England "own" a quarter of the earth and sit at ease while the "enslaved" races of the Empire sweat and work for the sole profit of the British people.

Hitler and his satellites know full well that what they say is false. The facts in the pamphlet speak for themselves, but how many of our own people, we wonder, have considered the significance of the following information contained in this leaflet? No part of the British Empire, it points out, pays taxes or tribute in any form to Britain. Every penny of the money raised by their taxes is spent upon the inhabitants themselves. Instead of drawing taxes from the colonies, the taxpayers of Britain help to keep them going. This year, in the middle of the greatest war in history, an Act of the British Parliament was passed providing that over £11 millions which had been loaned to the colonies in past years be converted into a free grant. The same Act provided that another £50 millions, spread over ten years, be given to the colonies to help them to develop their own resources and to improve their standards of living.

And what about the freedom of action of the people of our Empire? No part of the empire is obliged to buy what it needs from Britain or to sell its products to Britain. Full advantage is taken of this freedom and, as an example, the British colonies buy only 25 per cent of their imports from Britain, and more than half of their trade is with foreign countries. How many of us know that British India, which Hitler and Mussolini say is "owned" by the British people, buys less than one-third of her total imports from Britain? In the whole of British India, which has a population of about 275 millions, there are only 715 European civil servants and 450 officers of the police service. All the rest, numbering many thousands, are Indians, and even in the highest ranks Indians serve on terms of com-

plete equality with their British colleagues. Under the constitution, all the provinces of British India manage their own affairs, with elected parliaments and cabinets of Indian ministers who are responsible to these parliaments. Internal order and the defence of the north-west frontier against raiding tribes are maintained in peace time by a voluntary army of 210,000 officers and men with 34,000 reservists, and of these only 60,000 are British troops.

The members of this glorious commonwealth of nations should not weary in re-telling these facts but should broadcast them to the world. The British commonwealth is a gigantic experiment in internationalism. It consists of (a) a group of completely independent nations such as Canada, Australia, South Africa, New Zealand and Eire, working together in free association, (b) others, such as India and Burma, which are rapidly approaching the same status, and (c) a collection of colonies and protectorates which are being guided and assisted along the road towards a similar goal. It is a world-wide association, including white, brown, yellow and black member-states. Its basis is not, as Hitler and Mussolini would have the world believe, tyranny and exploitation, but liberty and progress and the privilege to all peoples of enjoying the beauty and abundance which Mother Earth provides with a lavish hand.

Loyalty Indefinable

No wonder then that when Great Britain took her stand on the side of the weak nations of Europe a year ago, the members of this vast commonwealth rose to take their place by her side. Loyalty is an indefinable thing; here is a time when our *Concise Oxford Dictionary* has failed us, and we find ourselves forced to turn to the treasuries of our literature for a suitable description. But where are to be found the choicest illustrations of the feelings and aspirations of the mind and the heart of man? One of the most unfortunate things, we think, in the modern system of education is that the rarest gem of our literature became linked with religious denominationalism, and in consequence the public schools throughout this wide Dominion became robbed of the beauties of description and the poetic cadences of the Bible. No other great literary work can approach it. We know that there will be a few of our readers who even yet will take exception to our reference to this literary pro-

duction of many centuries ago but, as an illustration, where else in our literature can be found a passage comparable to the 137th Psalm in its outpourings of patriotism and loyalty? And should the individual, whoever or whatever he may be, become puffed up, and should the flower of patriotism in any nation for some reason or other fail to shed its full fragance for the enjoyment of other peoples, what else in literature can compare with the test for self-examination to be found in the thirteenth instalment of the first letter which Paul wrote to the people of Corinth nineteen centuries ago?

In the Middle Ages the Bible was the text book of literature. It breathes through the writings of Addison and Shakespeare and Milton and it is doubtful if without its beauties Shakespeare could have put into the mouth of old John of Gaunt those expressions of loyalty to the land of his birth which will be read and cherished down the ages wherever the English language is spoken, and when the names of Hitler and Mussolini like that of Napoleon will long have become unsavoury memories:

> This royal throne of kings, this scepter'd isle
> This earth of majesty, this seat of Mars,
> This other Eden, demi-paradise;
> This fortress built by Nature for herself
> Against infection and the hand of war;
> This happy breed of men, this little world;
> This precious stone set in the silver sea,
> Which serves it in the office of a wall,
> Or as a moat defensive to a house,
> Against the envy of less happier lands;
> This blessed plot, this earth, this realm . . .
> This land of such dear souls, this dear dear land,
> Dear for her reputation through the world.

PRESIDENT'S ADDRESS

DURING our last annual meeting in Saskatoon in the latter part of August 1939, the war clouds were gathering rapidly in Europe and before many of us had returned to our homes they had broken over Poland with devastating effect. Since then we have viewed a series of developments which have profoundly shocked us into a realization of the danger which confronts civilization until now the British Empire is fighting, almost alone, for the preservation of liberty and freedom and all that is decent in human relationships. How, where or when our enemy will be defeated we do not know. Our sacrifices will be great and we have many ordeals ahead of us but we have no doubt of the ultimate victory.

It is sometimes difficult to deal with the affairs of our Association and with our everyday work when all these things seem so unimportant compared with our main effort of seeing this war through to a successful conclusion. We must, however, carry out our daily tasks as best as possible and lay plans for the future. In so doing we manifest our belief in the eventual outcome.

In the early part of this year we had planned to hold our meeting on the usual scale, including sessions devoted to the presentation of papers and roundtable discussions in addition to the usual social functions which have been held in the past. With the serious turn of events in May, however, our Executive Committee, with the ready concurrence of the Society of Chartered Accountants of the Province of Quebec, decided to limit our proceedings to sessions of council and a meeting of members at which the work of the past year would be considered and reported upon. The action of the Quebec Society in donating a sum of $2,500.00 to the Dominion government, which would otherwise have been spent on these social functions, has been warmly commended by our members across Canada. In similar manner other Provincial Institutes and student bodies have curtailed social activities and have donated the savings so effected to the Canadian Red Cross and other war charities.

---

*Address of Kenneth W. Dalglish, C.A., President of The Dominion Association of Chartered Accountants, delivered at the Thirty-Eighth Annual Meeting of the Association, Montreal, 5th September 1940.

At past annual meetings we have had the privilege of having with us representatives of the Institute of Chartered Accountants of England and Wales, the American Institute of Accountants and other accounting bodies. Due to the war and to the restricted nature of our proceedings they are not with us this year but we hope that it will not be long before we are able to have them with us again. Our thoughts very naturally go out particularly to the members of our profession in the Mother Country, who, along with others there, are undergoing the present ordeal. A number of our members have shown their sympathy in a practical manner by offering to take children of old country chartered accountants into their homes for the duration of the war. Our Association is now in communication with the societies of practising accountants in England and Scotland and it is hoped that suitable arrangements will be completed at an early date.

Like all others, our profession has felt the force of the war, although it is only now that we are beginning to experience the full effect. To a large extent we have been able to carry on in our normal way and during the past winter we have experienced comparatively little dislocation of our work. Many of our members and students, however, are now on active service with His Majesty's Forces and others are on the staffs of the Foreign Exchange Control Board and other departments of the government. In addition many are devoting part of their time to military duties in the Non-Permanent Active Militia and all our younger members and students will eventually undergo a period of military training.

We will not be immune, nor do we expect immunity, from the full force of the war and it will be increasingly difficult to carry out the regular work of our profession. In Great Britain women have been employed to some extent in the offices of practising firms to undertake work previously done by junior staff, and those partners and seniors remaining are working long hours. It will occasion no surprise if we are faced in due course with a similar situation to which we will require to adjust ourselves.

We are gratified at the part which members of our profession are playing in the service of the Dominion government. Many are acting in capacities where trained

minds and accounting and financial knowledge are essential. In this connection we may make special mention of the Foreign Exchange Control Board which has functioned in a manner so very acceptable to business and to a public entirely unaccustomed to measures of that kind. Over fifty qualified chartered accountants are now on the staff of the Board.

The demand for qualified accountants by various departments of the Dominion government is increasing. We welcome the recognition so given to our profession and we are glad to see qualified chartered accountants in positions where their training and knowledge can be used to the fullest advantage. It is to be hoped, however, that the government will not engage chartered accountants for work which can be adequately carried out by others with lesser qualifications. With the advent of the Excess Profits Tax and other war measures our profession will be in need of well qualified men. To the extent that proper financial accounts form the basis of a determination of taxes, our profession, apart from its other activities, is engaged in work of national importance in assisting in their preparation. It is to be hoped, therefore, that our profession will not be unduly depleted and that we will have adequate qualified staffs left to carry on.

Uniform Examinations—It is not my intention to dwell at any length upon the activities of our Association during the past year as these will be reported upon to you in the form of reports of the Council and of the various committees. However, I would like to make mention of some of the noteworthy developments. Foremost among these was the holding of uniform examinations in accounting and auditing, both in the intermediate and final examinations, last December, at which three hundred and forty-nine candidates sat. All of the Provincial Institutes except one, namely, the Institute of Chartered Accountants of Saskatchewan, participated in these examinations and the way is now clear for that Institute to arrange for their students to sit the uniform examinations this coming December. Arrangements are now being discussed which we hope will result in the French-speaking students in the Province of Quebec writing the same papers after they have been translated into French. The holding of these uniform

examinations may be considered one of the outstanding achievements of our Association since its inception. Our profession owes a debt of gratitude to many of our members who through their untiring efforts over a number of years have made these uniform examinations possible. This forward step has only been accomplished through each of the Provincial Institutes meeting the whole scheme in a spirit of co-operation because it has necessarily entailed a variation in the usual examination arrangements of each Institute. A very large amount of work was thrown upon the Secretary's office but it was carried out by Mr. Carr and his staff with characteristic thoroughness and despatch.

The Magazine of the Profession—"The Canadian Chartered Accountant" has maintained its place in the literature of our profession and is now a publication of which we can be proud. It is to be regretted, however, that more original material from our own members is not forthcoming. It does, admittedly, require time and effort to write an article for publication and many may not have the aptitude for writing which others possess. However, there is no reason why there should not be an adequate number of articles tendered at all times and I trust that during the coming year we may be favoured by material for the magazine from the pen of some of our more experienced members.

Our Association has continued the distribution of tax and other information, including the summaries of Dominion and Provincial taxes and of the judgments rendered in income tax cases before the Exchequer and Supreme Courts of Canada. In addition to the distribution of this information our members, during the past several months, have had the rulings of the Foreign Exchange Control Board sent to them and these have proved to be valuable sources of information and reference.

A committee was appointed early in the year to consider *The Excess Profits Tax Act* which was passed at the Session of Parliament called in September 1939. Our committee held a number of meetings in Montreal and Toronto as a result of which a memorandum containing the suggestions of our Association was drafted. Representatives of our committee were privileged to submit this memorandum at an interview held with the Minister of National Revenue

and officers from the Income Tax Department last January when its contents were given careful consideration. The new Excess Profits Tax Act recently enacted gives effect to quite a few of the suggestions tendered at that time.

Accounting Research — The war, of course, has made necessary the restriction of some of our activities which in normal times were of some importance. I refer particularly to our programme of accounting research which was instituted in recent years and which was being carried on in conjunction with the staff of Queen's University. It will be appreciated that it will not be possible to devote the time to this work which is deserved and which by its very nature must be carried on in a sustained manner over a long period. We have been very fortunate, however, through the kindness of our friends, the American Institute of Accountants, in having available the results of their studies in research. We are very grateful for the permission given to us to publish their Research Bulletins in "The Canadian Chartered Accountant."

At recent annual meetings the attention of our members has been directed towards the form of auditor's report to the shareholders, arising out of the variation in wording now prevalent. During the past year our Association asked each Provincial Institute to appoint a committee to study this important matter with a view to determining as to whether or not it was desirable that a uniform form of unqualified auditor's report be recommended for adoption in Canada. These committees have now reported to their respective Councils and their reports are now in the hands of a committee of our Association for further study.

Taxation—It would seem to be appropriate that some of my remarks should be devoted to the field of taxation, which plays an ever increasing part in the practice of our profession.

The budget brought down in July by the Dominion government involves additional taxation on an unprecedented scale which will be borne by almost everybody. The lowering of the statutory exemptions under the *Income War Tax Act* and the application of the national defence tax to even smaller incomes will involve the payment of taxes on income on the part of small wage-earners hitherto exempt. Such direct taxation is to be commended as it brings

home to the small wage-earner an awareness of the cost of the war and of government which would not be present under methods of indirect taxation. The increase in the rates of income tax, particularly on moderate incomes, is very heavy and everyone will be called upon to contribute to the cost of the war effort. These increased taxes have been received by business and the public alike without complaint but there is a definite feeling that government expenditures which may have been highly desirable in times of peace, but which are not now essential, should be curtailed. There may also be a tendency on the part of taxing authorities not connected with the war effort to take advantage of the receptive minds of the public towards increased taxation. Added taxes of this nature in war time, unless absolutely necessary, are to be deplored and are bound to bring unfavourable reaction in their wake.

The Sirois Report—As the war progresses, and we have been warned that it will not terminate in a short time, it will be necessary for the Dominion government to find increasing annual revenue to finance our growing war expenditures. It is essential that the reservoirs of national income be tapped as little as possible by other taxing bodies if we wish to finance the greater part of our war effort out of current income. The report of the Royal Commission on Dominion-Provincial Relations has now been made. It is somewhat unfortunate that a document of such far-reaching proportions should have come before us in these critical days when in times of peace it would have received the undivided attention of the whole Dominion.

Members of our profession, possibly more than any other body in Canada, are aware of the multiplicity and overlapping of taxes on income and capital levied by Provincial and Municipal authorities. Among the recommendations of the Sirois Commission is one whereby the Dominion government should take over the sole right to levy corporate taxes, income taxes and succession duties. The provinces would, in turn, be relieved of a great deal of their present burdens. This is a recommendation with which our whole profession will be in complete accord. The simplification of our taxation structure in Canada is long overdue and we hope that the recommendations of the Royal Commission will not be shelved indefinitely. There is now a body of

public opinion which advocates the implementation of its more important recommendations at the earliest opportunity as a means towards an even greater degree of national unity at this time coupled with the necessity of arranging our economy to meet the war effort and the financial problems which will face us immediately at its conclusion. I believe that this report should receive the attention and study of our profession during the coming year and it is to be hoped that our Dominion Association and Provincial Institutes will appoint committees as soon as possible to consider these important recommendations.

Problems of the Future—It is to be expected that a President on the eve of his retirement should, out of the experience of his office, have some suggestions to make regarding activities which might properly be undertaken by the Association in the future. Measured in terms of years since the formation of our Provincial Institutes, our profession is a comparatively young one and our growth, particularly during the past twenty years, has been very rapid. We possibly have not had the time to review our development in retrospect. Except for the papers and round-table discussions at annual meetings there has been little opportunity given for an interchange of views on our procedure in accounting and auditing. Our programme of accounting research upon which we had embarked had, as one of its principal objects, the undertaking of studies which would have revealed the current methods of accounting treatment, particularly in the preparation of annual accounts. I believe that the time has come when we should endeavour to arrive at a better understanding of accepted accounting and auditing practices with a view to accomplishing a greater degree of uniformity. During the past year an attempt has been made to commence work of this nature in ascertaining the views of the profession on the form of the auditor's report to the shareholders. It is, I believe, in this field that the Dominion Association has a future opportunity of rendering even greater service to our profession.

Our work may have to be postponed to a large extent until less troublous times return but eventually I hope that our Association through the time and effort of individual members will give leadership to these matters.

In the meantime, I am satisfied that the Dominion Association through its present activities is rendering many valuable services to our profession. We can claim many accomplishments during the past ten years and these have been due in no small measure to the devotion and untiring efforts of our Secretary, Mr. Carr, in looking after the affairs of our Association.

THE LAKE SHIPPERS' CLEARANCE ASSOCIATION*

By William H. Gray, B.Com., Winnipeg

THE Lake Shippers' Clearance Association is a very unusual organization designed to coördinate the handling of grain at the head of the Great Lakes. It was formed by the grain shippers in September 1909 as a co-operative nonincorporated mutual association. A short sketch of some aspects of the grain trade is necessary to a full understanding of the part played by this Association.

Since most of the grain grown on the western prairies is destined for export to Europe, its first movement is by rail from thousands of country elevators to the great terminal elevators at Fort William and Port Arthur. From there the easterly movement is principally *via* the Great Lakes and the St. Lawrence River canal system to the Atlantic seaboard, or by boat to the American lake ports, where the grain may be trans-shipped by rail to the coast. Since the grain is in its first really marketable position when it arrives in store in the Lakehead terminals at Fort William and Port Arthur, great storage facilities have grown up there. Owing, however, to its more favourable location with respect to the producers, Winnipeg has become the scene of the primary grain market and the Winnipeg Grain Exchange is recognized as the world's largest cash grain market. It is a peculiar situation existing nowhere else in the world, that here is a large public market for dealing in grain situated four hundred miles away from the warehouses or elevators where the grain itself is stored for delivery on sales.

Trading on the Winnipeg Grain Exchange is carried on

*This article is part of a thesis on "The Functions and Operations of The Winnipeg Grain Exchange" submitted in 1939-40 to Queen's University, Kingston, in the course leading to the degree of Bachelor of Commerce.

without the appearance of any actual grain, by the use of warehouse receipts (Form 1) issued by Lakehead terminal elevators. Strict regulations by the Exchange and by the Board of Grain Commissioners for Canada ensure that prompt delivery of grain of government grade and weight will be made upon the presentation to the issuing elevators of registered warehouse receipts.

Possessors of warehouse receipts who wish to make shipments surrender their documents to the Clearance Association, which acts as a clearing house, combining the grain documents of different shippers and re-arranging them so as to facilitate the loading of cargoes on vessels and the loading of cars for rail shipments. The importance of this function may be appreciated by supposing that the Clearance Association does not exist today. There are twenty-seven terminal elevators on the water front at Fort William and Port Arthur, each of which issues warehouse receipts which are deliverable on any purchase of grain in the Exchange. Thus a shipper buying a large quantity of cash grain may come into possession of warehouse receipts issued by every elevator on the water front. Without a clearing house, the shipper would have to send his vessel to every one of these elevators, taking on a small load at each. This naturally would be an excessive waste of time and energy, especially if every other shipper were in the same position, and would result in a higher freight rate and the loss of interest and storage charges through delay.

The function of the clearing house may be illustrated by an example. Suppose that five firms, A, B, C, D and E have shipments to make of varying amounts of Number One Northern wheat. Assume that the amounts of the shipments and the warehouse receipts held by each are as follows:

	Pool 4	*Empire*	*Reliance*	*Eastern*	*Ogilvie*	*Total (bushels)*
A	40,000	20,000	.....	10,000	10,000	80,000
B	10,000	.....	31,000	9,000	.....	50,000
C	10,000	15,000	1,000	11,000	3,000	40,000
D	10,000	5,000	4,000	10,000	41,000	70,000
E	10,000	10,000	4,000	30,000	6,000	60,000
	80,000	50,000	40,000	70,000	60,000	

Without the clearing house, A's vessel would have to make four calls, B's three, C's five, D's five and E's five. It is obvious, however, that if all the documents are pooled

the same results would be obtained if A's vessel were sent directly to Pool No. 4 Elevator, B's to the Empire Elevator, C's to the Reliance Elevator, D's to the Eastern Elevator and E's to the Ogilvie Elevator. From the saving illustrated in this sample it is easily understood why the Association is of such value when there are twenty-seven elevators and several score shippers to deal with.

The same principle has been applied to the loading of railway cars. Combining the loading orders of a great many shippers enables a number of cars to be moved past one loading spout to load the same grade of grain; and trains can be handled without the necessity of having to load one car with one grade and then clean out the spout and load a car with another grade. The Clearance Association has been given complete charge of the distribution of cars for all Eastern shipments with full authority from the railways. There is considerable saving to the railways since all cars can be loaded to full capacity and switching is reduced to a minimum.

In addition to its clearing function, the Association performs other valuable services. It acts as a trustee for the banks by holding grain warehouse receipts—upon the security of which the banks have advanced money—until they are replaced by rail or vessel bills of lading. It receives the shipping order from the shipper, loads out the grain according to the terms of the order, makes out the bills of lading in split quantities as required, receives the government weight and grade certificates to correspond with these bills of lading, makes out all required customs papers including export entries and consular invoices, and delivers all these documents to the shipper or his bank. As well, it pays all the storage, elevating, inspection and other fees against the shipment, and bills the shipper for them on a detailed manifest. It maintains a private wire between its Winnipeg and Fort William offices so that all instructions of the shippers with regard to changing loading orders, destination, billing, and so forth can be easily carried out. The Association, obviously, has a position of great responsibility, and its system is wonderfully organized to afford the utmost safety and accuracy. It has the full legal control of millions of dollars worth of grain and very careful accounting records must be kept. These records are unusual in that

they are nearly all in terms of bushels and pounds rather than money.

When a shipper is planning to make a shipment, he deposits warehouse receipts with the Association. He lists them on forms known as surrender sheets (Form 2) in chronological order of the date of storage, and enters full particulars as to the number of bushels, the grade and the date stored. Four copies of these sheets must be submitted, along with three copies of deposit slips (Form 3) on which are listed the warehouse receipts with the name of the elevator, the grade and the number of bushels. Deposit slips are usually made out to the shipper's bank. The warehouse receipts are checked against these lists. One copy of the deposit slip is retained in the shippers' ledger department on file, while the other two copies are signed by the Association and returned as receipts for the warehouse receipts, one to the bank and one (marked "duplicate") to the shipper. A pro[1] number is assigned to and marked on the surrender sheets and warehouse receipts for a filing reference, and this number is entered in the pro register with the date, the shipper's name, the number of bushels and the type of grain. Of the surrender sheets, two copies are used for the entries in the shippers' ledger and then filed in the shipper's file of the shippers' manifesting department. The third copy is filed in the elevator manifesting department and the fourth is mailed to Fort William. The shippers' ledger has accounts for every shipper, indicating the date of entry and the grain, grade and bushels of the warehouse receipts on deposit by every shipper. The elevator ledger has accounts for every Lakehead elevator, showing the date of entry and the grain, grade and bushels represented by the warehouse receipts held by the Association. The warehouse receipts are filed in the vault under the names of the elevators. The shippers' ledger is the record of grain on call by each shipper from the Association and the elevator ledger is the record of grain on call by the Association from each Lakehead elevator. Obviously these two must balance exactly.

The warehouse receipts are then listed by elevators on forms known as confirmation slips (Form 4) of which five copies are made. One copy is used for the entries in the

[1]Trade term applied to reference numbers.

elevator ledger. A second copy is retained by the operator who telegraphs the facts on it to the Fort William office for entry in the duplicate elevator ledger there; and a third copy is mailed to Fort William as a confirmation. The other two copies are sent to the elevator companies to notify them that they have outstanding warehouse receipts in the hands of the Association.

When the shipper has completed his arrangements, he sends the Association orders as to what grain to ship, when, and by what vessel. At the same time a notice comes from the vessel agent confirming the name of the vessel and the date it can load. These instructions are wired to the Fort William office. A short time later the Fort William office wires back, stating the amounts they will load from each elevator.

The shippers' ledger department file is next consulted. In it, under each shipper's name, are the surrender sheets submitted originally with the warehouse receipts, and at this time surrender sheets are selected which list warehouse receipts to the total of the amount being shipped. If only some of the warehouse receipts on a surrender sheet are required, or if only part of a particular warehouse receipt is needed, the extra amount is crossed off that sheet and entered on a new sheet which goes back, with a copy, into the file. This shippers' file remains as a reference in support of the balance in the shippers' ledger.

Complications arise in the clearing system due to the fact that storage charges begin to accrue on all warehouse receipts fifteen days after they are issued, at the rate of one thirtieth of a cent per bushel per day. Since the warehouse receipts deposited by the shippers are not the same ones surrendered to the elevators for that shipment, the shipper must pay the storage charges accrued on his warehouse receipts up to the date of shipment, while the Association pays to the elevators the charges accrued to date on the warehouse receipts actually surrendered.

On the two copies of the surrender sheets selected, storage charges are computed and entered. One copy is filed while the other is sent to the shipper with a manifest (Form 5) showing the storage, elevation, warehouse receipt cancellation, weighing and inspection and Clearance Association charges. Elevation charges are 1¼ cents per bushel, weigh-

ing and inspection $2.00 per thousand bushels, cancellation charges 4 cents per thousand, and Clearance Association charges 30 cents per thousand. The shipper pays these immediately by cheque.

When the Fort William office wires the exact amount of the shipment, the shipper's ledger account is reduced by this amount. This completes the entries in the shippers' ledger department.

When the wire first comes from Fort William stating the quantities to be loaded from each elevator, warehouse receipts are selected up to the approximate amounts required from each elevator. They are listed on a surrender sheet form and sent to the Winnipeg office of the elevator company. This list is signed by the company and returned to the Association as a receipt for the warehouse receipts. The Association has an adjustment ledger in which each elevator company is charged with the amount of the warehouse receipts sent to it. This amount is not entered in the elevator ledger because the exact amount of grain shipped is not yet known. The adjustment ledger entry is merely of a temporary character.

When loading has been completed, the Fort William office wires back the exact weights according to the government certificate. The elevator company returns to the Association the warehouse receipts it has been given in excess of the amount shipped. When part of the grain represented by a particular warehouse receipt is used to make up the exact total, then splits are issued and registered in place of the original warehouse receipt, and the split warehouse receipt for the excess amount is returned to the Association. The elevator's account in the adjustment ledger is credited with the amount loaded plus the amount of the warehouse receipts returned, and this closes the account. At the same time, the elevator's ledger account is reduced by the exact amount of the shipment. The total of accounts in the elevator ledger is again in balance with the total in the shippers' ledger.

The elevator company sends the warehouse receipts to the registry office for cancellation and makes up an elevator manifest charging the Association for all charges accrued on these warehouse receipts for storage, cancellation, elevation, weighing and inspection. The Association pays this

charge immediately by cheque. It is clear that the charges collected from the shipper on the shipper's manifest and the charges paid to the elevator company on the elevator manifest will not be in agreement for each transaction, because the accrued storage will differ owing to the use of different warehouse receipts. In the long run, however, they will balance out in total.

The Fort William office makes up the original bills of lading for every shipment and, for rail shipments, has them signed by the railway company. The Association has authority to sign vessel bills of lading on behalf of the vessel companies. The bills of lading, accompanied by government weight and grade certificates and the required customs papers, are sent to the Winnipeg office with the detailed shipment report indicating the grain, weight, grade, vessel destination, and elevators loaded from. The bills of lading and documents are turned over to the shipper or the shipper's bank in return for a signed receipt which the Association retains.

This is the normal course of business, but sometimes a shipper may wish to sell grain after he has deposited the warehouse receipts for it with the Association. Obviously the Association cannot return him his own warehouse receipts since they may have been used for someone else's shipment. In this case, the shipper fills out a transfer requisition (Form 6) and from it the Association issues him a transfer certificate (Form 7) which indicates that he has at his credit grain of a certain weight and grade. This amount is charged against his account in the shippers' ledger and credited to transfer account. The requisitions are filed by grain and grade and equal in total the balance of the transfer account. Before the certificate is issued, the Association makes up a transfer manifest (Form 8) on which is charged storage accrued on the original warehouse receipts up to five days after date of the manifest, and this charge is collected from the shipper. The surrender sheets for the original warehouse receipts are removed from the shippers' file when the transfer manifest is made out, or else warehouse receipts are simply marked off the surrender sheets to the amount of the transfer. The surrender sheets in this file must at all times balance with the shippers' ledger. Transfer certificates may change hands indefinite-

ly by endorsement and, though not mentioned before, they rank equally with registered warehouse receipts and may be used for delivery upon any contract made in the Exchange. They are a very convenient form to use for making deliveries, since they obviate the need of adjusting with the purchaser for the accrued storage on a number of warehouse receipts.

The new owner of a transfer certificate may wish to surrender it to the Association in anticipation of a shipment. When he does so, his account in the shippers' ledger is credited, and transfer account is debited by the amount of the certificate. The original requisition form is removed from the file and put away with the cancelled certificate. Surrender sheets go into the shippers' file, bearing the date of the certificate for storage charge purposes.

A transfer certificate does not meet the need of parties who wish to withdraw actual warehouse receipts. Sometimes a shipper will want them, but more likely it will be an elevator company which has been notified on a confirmation sheet that some of its outstanding warehouse receipts are in the hands of the Association. It may desire to have the grain left in its elevator where it will earn storage charges. In such cases it may purchase similar warehouse receipts of some other elevator company and surrender them to the Association in place of its own. Accrued storage is figured on the two groups of warehouse receipts, on a withdrawal form (Form 9), and the Association pays to the elevator company the excess of storage due on the elevator company paper over that due on the new paper surrendered, or collects from the elevator company if the excess is the other way. A small withdrawal charge is made.

All the financial transactions of the Association are for cash and go through a cash journal with columns for bank, shippers' manifest charges received, elevator manifest charges paid, withdrawals and sundries. The totals of the manifest columns are split up at the month end according to a recapitulation of the actual manifests, and postings are made to various accounts for storage, commissions, elevation, warehouse receipt cancellations, weighing and inspection charges. The withdrawals account includes accrued storage paid and received and a small credit for with-

drawal charges. This account is closed out into the storage and withdrawal charges accounts.

The Fort William office operates as a branch, with its own accounting system. It collects commissions from vessels at different rates which vary inversely as the time taken by a vessel at a terminal from the moment it starts to load to when it finishes loading. The fewer terminals a vessel must visit, of course, the less time is spent and the higher the charge it must pay. This method of charging commissions is satisfactory to the vessel owners because they can make a considerable money saving if the time spent on loading is reduced; it also encourages the most efficient operation of the Association.

The Lake Shippers' Clearance Association is an outstanding example of a co-operative organization which was developed in response to a definite pressing need. It is admirably suited to its purpose and, indeed, those in contact with it are unanimous in declaring that the Association is an absolute necessity to the swift and economic movement of the tremendous annual volume of grain from the Lakehead.

Note: The Forms referred to in this article appear on pages 240-245.

FORM 1—WAREHOUSE RECEIPT

BLANK GRAIN COMPANY LIMITED

WAREHOUSE RECEIPT

No...........

Received in Store in Our Port Arthur Elevator, Subject to the Order of

....

Grain of grade and quantity as shown hereon. Like grade and quantity will be delivered to the holder hereof upon surrender of this receipt properly endorsed, and on payment of all lawful charges due to this company in connection therewith.

Storage in arrears against this grain in excess of 30 days shall be paid at the office of this company February 15 and August 15 in each year.

This receipt not valid unless Signed, Countersigned and Registered.

Date of Issue ....

Grade ....
Bushels ....
Pro .... Car ....
Received into
Store ....
Accrued Storage Paid to:
.... Certified ....
.... " ....
.... " ....

Blank Grain
Company Limited

By ....

Countersigned
By..................................
Registered as to weight and grade

FORM 2—SURRENDER SHEET

N.B.—L.S.C.A. requires 4 copies (typewritten preferred). Put only one grade on a sheet. Arrange W.H.R.'s in order of date of storage.

LAKE SHIPPERS' CLEARANCE ASSOCIATION

SURRENDER SHEET

Grade .... *No.* ....

For Account of .... *Date* ....

Issue Deposit Receipt for Same to the Order of ....

ELEVATOR ....

	Ship. Ref.	W.H.R. No.	Bushels	Lbs.	Date Stored	Year	Days	Storage Charges	Disposition
1 2 Etc.									

Delivery in pursuance of such deposit receipt shall be in full satisfaction and discharge of all liability of the Association.

....

Firm's Signature

RECEIVED from LAKE SHIPPERS' CLEARANCE ASSOCIATION Warehouse Receipts as per the above list subject to call and shipping instructions of the said Association.

Signed ....

Elevator Signature

FORM 3—DEPOSIT SLIP

Winnipeg, ...19.....

Deposited with Lake Shippers' Clearance Association registered warehouse receipts and/or Transfer Certificates covering grain as per list below:

The Association will, at its option, either ship a like quantity and grade or deliver registered warehouse receipts therefor to

The order of ....
and such delivery or shipment shall be in full satisfaction and discharge of all liability hereunder.

Account ....

ELEVATOR	GRADE	BUSHELS	Lbs.

Received the above documents

LAKE SHIPPERS' CLEARANCE ASSOCIATION

Per..........................

Form 4—Confirmation Slip

Winnipeg, ... 19.....

.... ELEVATOR CO.

Summary of Registered Warehouse Receipts Subject to Orders From

LAKE SHIPPERS' CLEARANCE ASSOCIATION

Grain as per Attached Receipts

PRO.	GRADE	SHIPPER	BUSHELS	LBS.

Form 5—Manifest

LAKE SHIPPERS' CLEARANCE ASSOCIATION

MANIFEST

Winnipeg, ... 19....

Firm .... Account ....

Statement of Shipment on S.S. .... Report No. ....

Grade .... Bushels ....

Date .... Manifest Dept. No ...... Amount Manifested ....

PRO.	Charges	PRO.	Charges
		Total Storage	
		Elevation Charges 1¼c per Bushel	
		Outward Inspections and Weighing $2.00 per M...	
		W.R. Cancellation Charge 4c per M	
		Clearance Association Charges 30c per M	
		Car Lining $4.00 per Car	
E.&O.E.		Your Check	

FORM 6—TRANSFER REQUISITION

LAKE SHIPPERS' CLEARANCE ASSOCIATION

No.......

REQUISITION FOR TRANSFER CERTIFICATE

GRADE.............

WINNIPEG, ...19.... BUSH................

Please issue Lake Shippers' Transfer Certificate

to the order of ....OURSELVES..............................

for ....bushels of ....

Quantity

and charge same to our account,
manifesting us with accrued storage to ....19....

SIGNED........................ SIGNED........................

Bank's Signature Firm's Signature

If registered warehouse receipts and/or transfer certificates for grain in question have been deposited to the order of a bank this requisition must be signed by such bank before being presented to the association.

FORM 7—TRANSFER CERTIFICATE

LAKE SHIPPERS' CLEARANCE ASSOCIATION

TRANSFER CERTIFICATE

No. ....
Grade ....
Bushels ....
Storage Date.....

Winnipeg ....

This is to certify that this Association holds Registered Terminal Warehouse Receipts from Terminal Elevators, recognized as "Regular" by The Winnipeg Grain Exchange, covering

.... Bushels of ....
which will be delivered to the order of ....

The Grain represented by this Certificate is deliverable only upon the return of this Certificate properly endorsed and upon payment of all Terminal and Storage charges from ....

This Certificate may, upon being returned properly endorsed, be exchanged for Registered Warehouse Receipts, covering the said quantity and grade of grain, upon a proper adjustment being made of all Terminal and Storage charges as between the dates shown on such Warehouse Receipts and the date shown upon this Certificate and upon payment by the holder or the Clearance Association (as the case may be) of any difference in amount disclosed on such adjustment.

Countersigned ....

LAKE SHIPPERS' CLEARANCE ASSOCIATION
Per ....
Manager

THIS CERTIFICATE MUST BE SIGNED AND COUNTERSIGNED.

FORM 8—TRANSFER MANIFEST

LAKE SHIPPERS' CLEARANCE ASSOCIATION

TRANSFER MANIFEST

Winnipeg, ...19....

Firm .... Account ....

Transfer No.	Grade	Bushels		Date		Manifest Dept. No.	Pro.	Storage	

Your Check

E.&O.E.

FORM 9—WITHDRAWAL FORM

LAKE SHIPPERS' CLEARANCE ASSOCIATION

To .... Withdrawal No. .... Grade .... Date ....

.... We hand you Warehouse Receipts as below Bushels .... Elevator ....

L.S.C.A. Pro.	Storage	L.S.C.A. Pro.	W.R. No.	Bushels	Lbs.	Date Stored	Year	Days	Storage	

Storage Due L.S.C.A. ....

L.S.C.A. Charges ....

Total ....

Less Storage Due Shipper ....

Total Due L.S.C.A. ....

Received Above W. H. R's. ....

Firm ....

Per ....

Storage Due Shipper ....

Less Due L.S.C.A. ....

Total Due Shipper ....

ONTARIO CORPORATIONS TAX

By Philip T. Clark, Chartered Accountant, Toronto, Ontario

THE subject of this article, Ontario Corporations Tax, is one which over many years has changed greatly in the extent and nature of its application. Accountants will necessarily become more and more interested in the taxation of corporations especially since the country is now gearing itself to a war economy, and the various governments of our country are searching for ever greater revenues.

The Province of Ontario imposes tax on corporations by *The Corporations Tax Act, 1939.* As a background to a study of this Act a brief history of Ontario corporations taxation will prove interesting.

Corporations taxation made its appearance in Ontario for the first time in 1899. Between that year and 1931 the following classes of companies were the only companies which were subject to provincial taxation: banks, insurance companies, loan companies, trust companies, railway companies, express companies, telegraph companies, telephone companies, sleeping car companies, gas companies, electric companies and street railway companies. The subject of taxation (i.e. the measure on which the tax is calculated) in each case was set out in 1899 and up to the present time has changed very slightly. Naturally rates of taxation based on these "subjects" have increased. In 1931 for the first time all ordinary mercantile companies and all mining companies, investment trusts, personal corporations, etc., became taxable.

Before examining the various "subjects" on which corporations tax is based the difference between direct and indirect taxation should be understood. Most accountants are aware that under the *British North America Act* the Provinces have the right to impose direct taxation but are prohibited from imposing any kind of indirect taxation, whereas the Dominion may impose any kind of taxation whether direct or indirect. John Stuart Mill has defined direct and indirect taxation as follows:

> A direct tax is one which is demanded from the very person who it is intended or desired to pay it.

An indirect tax is one which is demanded from one person in the expectation and intention that he shall indemnify himself at the expense of another.

Excise taxes, custom duties, sales taxes, all imposed by the Dominion government, are indirect taxes. The persons who pay them directly to the government add their amount to the price which would otherwise be charged to the consumer and thus collect the taxes from the consumer. The income tax imposed by the Dominion is a direct tax; it is paid by the individual who received the income and he cannot indemnify himself by passing it on to someone else. The corporations tax is a direct tax because it is imposed against a company in a manner whereby the company itself pays the tax for the privilege of doing business and such tax cannot be passed on to the customers of the company. It is an expense of the company doing business in exactly the same manner as rent, realty taxes, salaries and wages or any other expenses which the company has.

Measurement of Basis for Tax

The measure or "subject" on which a corporations tax may be calculated may be any measure at all. In *The Corporations Tax Act* of Ontario there are a great many measures used. There are, for instance, four measures in use in the case of banks: the paid-up capital stock, the reserve fund and undivided profits of the bank, its principal office in Ontario, and the number of additional offices which it has in Ontario. Insurance companies are taxed on the measure of the amount of gross premiums they receive in a year from policy-holders in Ontario. Railway companies are taxed on the measure of the number of miles of track which are operated in Ontario; they are also taxed on other measures if they own and operate hotels in Ontario. Telegraph companies are taxed on the measure of the total amount of money invested in their telegraph line and the works and plant connected therewith; telephone companies, on the measure of their paid-up capital stock; express companies, on the measure of the number of miles of railway over which they operate in Ontario; and sleeping car companies, on the measure of the amount of money invested in such cars in use in Ontario. All other incorporated companies are taxed on three basic measures: paid-up capital, the number of offices or places of business operated in Ontario, and net income.

It will be noted that quite a number of these measures are related to something which is only in Ontario, whereas others are related to something which is not necessarily only within Ontario. For example, a bank is taxed on the amount of its paid-up capital stock. It cannot be said that any bank has all its paid-up capital stock invested in Ontario. Each bank which does business in the province is subject to tax in Ontario and it was apparently deemed equitable that the paid-up capital stock of a bank should be used in each case. If the rate of tax to be calculated on the paid-up capital stock of a bank were 1% instead of 1/5 of 1%, the tax might be attacked in the courts on the basis that it would be confiscation. For instance, the tax imposed on banks by the government of Alberta in its Corporations Tax Act was attacked successfully on this basis. However, so long as it cannot be attacked in this way, such a tax imposed on banks is perfectly legal under the *British North America Act*, even though the Province of Ontario, as well as the Province of Quebec and several other provinces, use the same measure for the calculation of the tax in each case. Neither can it be said that, because the several provinces use the same measure on which to calculate the tax, the tax imposed by one province is a duplication of that imposed by another. If a bank does no business in Ontario, it will not be taxable in this province. If it does business in Ontario and also in another province, then each of the provinces is legally within its rights when it imposes a tax based on the same measure.

In the cases of special corporations already mentioned, the various bases are in most instances easily measured and, the amounts of such measures having been determined, there is little in the Act to complicate them. The same cannot be said regarding the various bases affecting all other incorporated companies.

There are three conditions any one of which, when applicable, makes a company taxable in Ontario: having its head or other office in Ontario, holding assets in Ontario, or transacting business in Ontario. Some companies have only an office in Ontario; it may be only a statutory office and the company may transact no business in Ontario at all but carry on its business elsewhere. On the other hand, it may not have an office in Ontario but it may hold assets

in Ontario and for this holding of assets it must pay a tax. The most common case is that all three conditions apply, that is, that a company has an office, transacts business and holds assets in Ontario.

Paid-Up Capital—The first basis or measure of taxation is paid-up capital, and the rate of this tax is 1/20 of 1%. The definition of paid-up capital in this part of the Act is not one which would be accepted by accountants as being the ordinary definition of paid-up capital. Paid-up capital generally would be considered to be the paid-up capital stock of the company, but the purpose of this taxing section is to use as a basis all kinds of capital, both paid-in and borrowed, as well as capital which arises from profits which have not been distributed amongst the shareholders. Therefore, the definition includes the company's paid-up capital stock, its earned surplus, its capital surplus and any other surplus and all its reserves except any reserve the creation of which is allowed as a charge against income under the income taxing provisions of the Act. There are also included all sums or credits advanced or loaned to the company by any other company and all indebtedness of the company represented by bonds, bond mortgages, debentures, income bonds, income debentures, mortgages, lien notes and any other indebtedness to which the property of the company is subject as security.

Paid-up capital stock and earned surplus may be easily understood without further discussion. On the other hand, the exclusion or inclusion of reserves is a broad question. The income tax provisions in the Act permit the creation of certain reserves, the most common being reserves for depreciation and reserves for bad debts. For instance, if a company has a building of brick construction, the rate of depreciation allowed is 2½% of the cost of the building. If the company writes off 5% in a year, it is ruled that only 2½% shall be allowed, and the difference is considered merely an appropriation from surplus and as such is, for the purposes of capital taxation, really part of the surplus and is in consequence included as part of the paid-up capital. The same situation applies with respect to bad debts. The usual allowance granted to companies under the income tax provisions is that it may provide out of profit and loss an amount sufficient to bring its reserve for bad debts to an amount equal to 10% of its accounts receivable at the

balance sheet date. If a company provides more than this amount, so that the reserve shown by its balance sheet equals, say, 15% of its accounts receivable, the department of the government administering the Act will disallow the excess of 5% as a charge against income and will consider that such excess is an appropriation from surplus and is in effect part of the surplus and therefore part of the paid-up capital subject to tax. This does not apply in every case, however. There are certain companies which actually do lose on the average more than 10% of their average accounts receivable each year and consequently are entitled to have a reserve of more than 10% of accounts receivable on the balance sheet date. The procedure in such a case is to determine the average annual percentage of accounts receivable which were considered by the company to be actually bad, and therefore written off. If this figure is more than 10% and is actually, say 15%, then a charge will be allowed against profit and loss of an amount sufficient to bring the reserve up to 15% of the accounts receivable on the balance sheet date; no part of the reserve will be considered as an appropriation from surplus, and therefore no part of the reserve will be included with the paid-up capital.

There are also other reserves which are considered to be paid-up capital, such as inventory reserves and appraisal reserves. Sometimes the appraisal reserves are described as appraisal surpluses. Regardless of what they are called it is considered that if they are set up on the books of the company, the company admits that it has such a reserve or surplus, and such reserve or surplus is included as part of the paid-up capital unless it can be shown that it was created out of profit and loss and that such creation should be allowed as a charge against profit and loss in the year in which it was created.

The next large class of items which is included as part of the paid-up capital is "all sums or credits advanced or loaned to the company by any other company." This situation arises usually when an American parent company incorporates a subsidiary in Ontario with paid-up capital stock authorized at, say, $40,000, and advances to its subsidiary cash or merchandise to the extent of, say, $1,000,000. The ordinary trade accounts payable appearing on a company's balance sheet represent in effect credits loaned to

the company by other incorporated companies, but it is not the intent of the Act to tax current trade accounts payable. In order to place ordinary companies on the same basis as those companies which are subsidiaries of American companies, it is necessary to determine what portion of the balance owing on the balance sheet date by the Ontario company to its American parent company is represented by purchases of merchandise or services within the usual credit terms given by the American parent to its other customers, and to deduct the amount of such purchases from the balance owing at the balance sheet date and to regard the remainder of the credit as a real capital loan advanced by the parent company so that the Ontario subsidiary may carry on business. This balance is included as part of the paid-up capital.

The last class of liability of an incorporated company which is deemed to be part of its paid-up capital is its indebtedness represented by bonds and mortgages and any other securities to which the company's property is subject. This class of indebtedness is included as part of the paid-up capital because it is really a capital liability. The company has the use of this money for a long period of time, and the money so borrowed is usually invested in capital assets without which it could not carry on business. Prior to 1934 this class of indebtedness was not included as part of the paid-up capital subject to tax, and it was found that certain companies had a distinct advantage over others because of this omission. For example, one company might issue preferred stock and use the money derived to build its plant, whereas another would have only a small amount of common stock and issue a bond mortgage the proceeds of which would be used for a similar purpose. In earlier days the former company would be required to pay a tax on its common stock as well as on its preferred stock, whereas the latter company would be required to pay a tax only on its common stock and not on the amount of the bond mortgage. The two companies were actually doing the same thing, only the class of security being different. In 1934 the Act was amended to bring in these long-term securities as part of the paid-up capital.

Exempted Companies—Following this discussion of what constitutes paid-up capital, there should be borne in mind

that although the first taxing section states that every incorporated company transacting business in Ontario, or which holds assets or has an office in Ontario, shall pay the tax calculated on paid-up capital, there are a series of companies which are specifically exempted. All of the companies such as banks, insurance companies and railways which are taxed under specific sections of the Act are exempt from the tax on capital imposed against ordinary incorporated companies. Besides these the following are exempt from tax on capital:

Companies whose assets consist entirely of shares and bonds and the obligations of other companies;

Companies in receivership, no part of whose property is used by the liquidator or receiver in transacting any of the business for which the company was incorporated;

Companies which have not commenced to transact business or which have ceased to transact business;

Companies which are incorporated without share capital;

Companies which are incorporated for religious, charitable, philanthropic, social or educational purposes;

Companies which are organized and operated on a co-operative basis; and

Companies such as railway companies which have no operations in Ontario but which have only an office there for the purpose of soliciting business for its system outside of Ontario.

None of the companies mentioned above is entirely exempted from taxes under the Act. They are either taxed under the specific taxing sections, as banks, insurance companies, railway companies, etc., or else they are taxed as though each of them had at least one place of business. Taxes on places of business will be dealt with later in this discussion.

Deductions From Paid-Up Capital

Having determined that the company is taxable on its paid-up capital and having determined the amount of the paid-up capital, there are certain deductions provided from the paid-up capital before the tax is to be calculated.

Goodwill—The first deduction mentioned is that for

goodwill or other intangible thing. Goodwill often appears on a balance sheet merely to balance the excess of the par value of capital stock issued over the tangible value of working assets which the company received when such capital stock was issued. Often goodwill appears where there are two classes of capital stock, preferred and common, the latter being all or for the most part issued for goodwill. In this manner, the shareholders receiving common stock of a company obtain and keep control of the company's destiny although such shareholders gave no tangible consideration to the company for this stock. *The Corporations Tax Act* recognizes this condition by providing that, regardless of how small are the profits of a company having goodwill, not more than 50% of such goodwill can be considered as having no value and therefore deductible from paid-up capital. The other 50% is considered to be worth at least its book value, because the shareholders keep control of the company by obtaining fully paid-up capital stock for no tangible consideration. Besides goodwill there are other intangible assets such as patents, trademarks and franchises, which are considered to be in the same category as goodwill. There is one difference, however: if trademarks, patents and franchises are acquired by the company for a tangible consideration and have a definite term of usefulness or life, then to the extent of such tangible consideration they are considered to be tangible and not intangible assets of the company, and no deduction as an intangible asset is allowed from paid-up capital. When dealing with the income tax provisions of the Act, the write-off of tangible and intangible assets will be discussed.

If a company has goodwill or an intangible asset, it is valued as follows:

The net income of the company available for dividends for the past five years is averaged and capitalized at 6%. To capitalize net income at 6%, the net income available for dividends is multipled by 100 and the product divided by 6. The amount of income which the resultant capital amount would produce at 6% would be the amount of net income actually available for dividends. If such resultant capital amount equals or exceeds the capital stock issued, it means that such capital stock, as was issued for goodwill, earned at least 6% and that such goodwill has a value equal at least to its book value. In this case no deduction is al-

lowed from capital for goodwill. If, on the other hand, such resultant capital is an amount smaller than the capital stock issued, the deficiency is the amount of paid-up capital issued for goodwill which earned nothing, let alone 6%, and the amount of such deficiency, subject to the maximum allowance of 50% of the book value of goodwill, is considered as being goodwill having no value and is deductible from paid-up capital.

Discount on Sale of Mining Shares—The second deduction from paid-up capital is discount allowed on the sale of shares of a mining company. Companies incorporated under Part XI of *The Companies Act* are mining companies, which are the only class of companies permitted to issue their shares at a discount. Whenever a mining company sells its shares at a discount, the amount of such discount is deductible from paid-up capital. Discount on shares will be discussed further when the special features of the taxation of the capital of mining companies are dealt with.

Certain Investments—The third deduction from paid-up capital is that allowed for investments which the company makes in the shares, bonds and obligations of other companies and in government and municipal bonds and debentures. The main purpose of this deduction is to prevent duplicate taxation under this Act of the same capital. If one company taxable under this Act invests some of its capital in the shares and bonds of another company also taxable under this Act, and if there were no deduction allowed to the first company for such investments, it would be taxable on capital that is also taxable in the hands of the second company. In the earlier discussion regarding paid-up capital it was seen that loans and advances to a company should be taken in as part thereof, but that current accounts payable should not be considered taxable. Likewise, where a company lends money to another company either in the form of cash, merchandise or services, such advance should be considered an investment in the obligations of another company provided that such advances are not current accounts receivable. Advances of merchandise or services for a term within the usual credit terms of the company making the advance are considered current accounts receivable, and are not recognized as investments. There are certain long term advances which are not recognized as investments. Cash on deposit in the bank may be

considered an advance to the bank, but a bank is not required to pay any larger tax under this Act by reason of larger deposits and therefore cash on deposit is not allowed as an investment. Many companies which are wholly-owned subsidiaries of foreign companies make large profits in Canada but because of income tax legislation in the foreign countries the parent company does not wish its Canadian subsidiary to declare dividends out of these profits. However, the parent company wishes the use of the money represented by these undistributed profits of the subsidiary. The subsidiary advances such money to the parent without interest or security and no income tax is payable either to Canada or Ontario or to the home country of the parent company. *The Corporations Tax Act* of Ontario recognized this condition by specifically excluding such advances from the allowance for investments.

The amount of the deduction for investments is calculated by multiplying the amount of the paid-up capital which remains after the deduction for goodwill, by a fraction, the numerator of which is the total of the cost of the allowable investments, and the denominator, the amount of the total assets. If the investments are carried at a value less than cost, the difference between the cost and the book value thereof is considered a capital reserve and is added to the balance sheet amount of the total assets as well as to the paid-up capital. If amongst the liabilities on the balance sheet there appear allowable reserves, such as reserves for depreciation and bad debts, these must be deducted from the balance sheet amount of the total assets for purposes of the investment deduction fraction.

Two other deductions allowed from paid-up capital have to do exclusively with companies engaged in mining and will be dealt with in the later discussion of the taxation of mining companies.

The Case of Real Estate Companies—The next deduction has to do with the paid-up capital of real estate companies. Up until three years ago real estate companies were taxed on their paid-up capital in the same manner as other companies. Because of generally continuous losses for several years it was decided to amend the Act to relieve real estate companies specially. The amount of this relief is measured in relation to the company's net income. It was

necessary to provide definitely what should constitute a real estate company. The deduction is therefore granted only to those companies whose only business is the holding of real estate for sale or rent. If a company holds real estate for sale or rent but also holds other things such as merchandise for sale or stocks and bonds for sale or income, it is not entitled to the deduction. Certain companies are considered to be real estate companies even though they hold other assets than real estate if the total cost of such other assets does not equal more than the accumulated reserve for depreciation against buildings held for sale or rent plus 5% of the gross assets of the company. This concession is necessary because, for example, if a company commences business by owning an apartment house for rent—in other words holding only assets for sale or rent—and, after charging proper depreciation and all other expenses, breaks even, it must have on hand, besides the apartment house, cash or other assets equal to the reserve for depreciation, and therefore must hold assets other than real estate for sale or rent. The additional 5% is permitted because no company can exist without a certain percentage of current assets in order to carry on from day to day. The Act provides that the deduction shall "equal that portion of paid-up capital which is in excess of an amount of capital of which the net income earned from the operation of the real estate business after depreciation but before deduction of interest and dividends on any of the obligations of the incorporated company which are included as its paid-up capital, would be 8%." This means that any portion of a real estate company's paid-up capital (including mortgages) which does not earn 8% in a year shall be exempt or, in other words, only so much of the paid-up capital of which the actual income earned is 8% shall be taxable. It will be noticed that the net income to be used for this calculation is not the same net income upon which is calculated the income tax. In order to put all real estate companies on the same basis (some have mortgages and mortgages must earn their interest as well as paid-up capital its dividends), it is necessary to add back to ordinary net income the charge included therein of mortgage interest and to capitalize the result at 8%. If the capitalization of such special net income equals or exceeds the full paid-up capital of the real estate company, then there is no deduction from

the paid-up capital. If, on the other hand, such capitalization totals less than the full paid-up capital, then the deficiency is deductible from the full paid-up capital and the balance is the taxable capital.

The Case of Companies in Liquidation—The next deduction is calculated in exactly the same manner as that for real estate companies but this one relates to companies whose property is in the hands of a liquidator, receiver or trustee. Where the property of such a company is not used for any of the purposes for which the company was incorporated, the paid-up capital is entirely exempt from tax. If it is so used, however, so much of the paid-up capital as earns a full 8% in the year is subject to tax.

Mining Companies

Dealing with mining companies it will be understood that these companies are in an entirely separate class from those already mentioned. Their treatment is so different that there is issued for them a separate form on which to calculate the tax payable. A mining company progresses through various stages. First the prospector stakes his claims, and certain work required by the Mining Act has to be done to develop these claims. Sometime during this process, if the claims appear to have probable value, a company is formed and the claims are turned over to it by the prospector in consideration of the issue to him of a certain number of fully paid shares of the company. Following this, further cash for the development of the property is obtained by the sale to the public of shares in the company (most probably at a discount). Having proved the property valuable, still further sales of shares will be made and with the resultant cash a shaft is sunk and a mill built, and the company commences actual production. Finally the company is successful enough that it commences to make a profit. As a special incentive to mining development, no mining company is taxable on its paid-up capital in any particular until a profit of $10,000 is made in any one year. This does not mean that it is entirely exempt from tax under *The Corporations Tax Act* but only from tax calculated on paid-up capital. Once a mining company makes a profit of $10,000 or more in one year it becomes subject to tax on paid-up capital.

Most mining companies show the properties which they

acquired from the prospectors at a value which equals the par value of the shares issued fully paid in consideration for them. But because other shares were issued to the public at a discount, it must be admitted that there is a certain amount of discount on shares included in the valuation of the properties. Mining companies are therefore required to calculate the average price at which shares were sold for cash and apply such price to those shares issued fully paid for properties. The difference between the book value of the properties and the average cash value of the shares issued for them is considered discount on such shares. This discount added to the actual discount on shares sold for cash is the first deduction from paid-up capital.

The second deduction is that for investments in the shares and bonds of other companies and the bonds and debentures of governments and municipalities. The amount of this deduction is determined in exactly the same manner as that to which any other company is entitled.

The third deduction is for the mining company's investment in its mining properties and its shaft and other plant pertaining directly to the mine, as distinguished from the mill or refinery and all other assets of the company. The purpose in granting this deduction is that every producing mining company is specially taxed by the Mining Tax Act of Ontario on the profits of the mine. They are not taxed under the Mining Tax Act on their profits earned as a result of refining their ore or from any other source. The portion of a mining company's paid-up capital which is to be deducted for the mining properties and mine plant is determined by multiplying the balance remaining of the paid-up capital after deducting the discount on shares and the allowance for investments by a fraction, the numerator of which is calculated as follows:

> the book value of mining properties minus the relative discount on shares plus the gross value of the mining plant before the deduction of any reserve for depreciation,

and the denominator of which is calculated as follows:

> the total assets as shown by the balance sheet before deduction of any reserves for depreciation, minus the total discount on shares, whether sold for cash or properties and minus the allowance for investments already deducted from paid-up capital.

The balance of the paid-up capital now remaining is the taxable capital.

(to be concluded in November issue)

THE ROWELL-SIROIS REPORT AND THE WAR

Editor's Note: This is another in a series of notes on economic subjects by Professor McQueen of the University of Manitoba.

ECONOMISTS in their writings continually exasperate laymen by distinguishing between the "short-run" and the "long-run" consequences of economic change. If these laymen studied physics they would be forced to distinguish between statics and dynamics and they would proceed no distance in the subject unless they kept this distinction in mind. The difference between long-run and short-run in economics is similar to and as important as the distinction between statics and dynamics in physics, and why laymen think that economics should be simpler than physics is a continuous source of amazement to trained economists.

The current discussion of the Canadian wheat problem and of the problem of the proper location of war industries illustrates the important difference between the short and the long-run. There is of course a very grave short-run problem concerning the current wheat surplus and what we are to do by way of supporting the producers of that surplus. There is however an equally grave long-run problem of how we are to transfer the labour and capital out of the wheat industry into other industries if our accustomed wheat markets are not again going to reappear. The short-run problem is one of keeping a whole region economically functioning for the present while the long-run problem is one concerning a possible transfer of economic resources.

The question of the proper location of war industries also illustrates the importance of the distinction between the long and the short-run. From the point of view of immediate production for war purposes existing plants should be worked to the full and new plants located where production may be most quickly and efficiently begun. Where however various locations so far as can be seen offer equal possibilities for quick and efficient production there is some place for a long-run consideration. In this connection the

Honourable Mr. Gardiner is reported in the press as follows: "We may make suggestions of suitable locations for such industries so that expansion may be balanced and there will not be too great an increase in one particular district. We must guard against post-war difficulties." As a general proposition there can be no objection to this statement but the deeper difficulty of course lies in assessing just what kind of a world we shall have with us in the post-war period. Balanced expansion is one thing for the pre-war Canada we knew but it may be a very different thing for the post-war Canada we do not know.

Another way of stating the real problem involved will be to ask what exactly is meant by arranging that "there will not be too great an increase in one particular district." We need not be so cynical as to suppose that the Minister meant that we must ever keep our eye on the post-war balance of political sectionalism for it is clear from the news report of the minister's speech that he had in mind some kind of post-war economic balance. We must not forget however that post-war Canada will certainly require a different relative balancing of her labour, land and capital resources than that which she previously had achieved. It may even conceivably be that the best organization of her resources may call for still greater concentration of activity in the industrialized central provinces. Balance in the short-run means bolstering an existing situation to get over an emergency; in the long-run it means a shifting of labour and capital away from those places in the economy where their productivity is less to those places where their productivity is greater. The working out of such a long-term balance ignores the artificial gridiron of provincial boundaries and it is certain that the relative prosperity of different parts of Canada will be altered in the process. It is certain too that the process will generate some depressed areas in our country. The long-run remedy for a depressed area is a shift of human and capital resources out from it but in the meantime, with the present distribution of revenues and functions between the Dominion and the provinces, the area may become incapable of carrying on the necessary activities of government. Of one thing only can we be certain, viz., the post-war Canada will be a changed Canada requiring shifts of labour and capital with depressed area problems as a consequence. On such grounds as these there

is an answer to those who object to the implementing during the war of the Rowell-Sirois report. With, on the one hand, the future of the great western industry so uncertain and with, on the other hand, the certainty of disturbances incidental to changing our economy from a war to a peace basis there would seem to be more and not less reason for implementing the report immediately.

R. McQUEEN.

20th September 1940.

WAR CONTRACTS DEPRECIATION BOARD

Order in Council issued at the Government House at Ottawa 27th August 1940 and published in "The Canada Gazette" 7th September 1940.

WHEREAS the Minister of National Revenue represents that contractors may not incur capital expenditures unless they are reasonably assured that an allowance in respect of depreciable assets, acquired or constructed for war purposes, will be allowed by way of special depreciation when determining income tax liability, over a period shorter than that which would be allowed due to ordinary wear and tear by use of the capital assets concerned, and therefore in the interests of Canada and the furtherance of the war effort, it is advisable that a Board with duties and powers as hereinafter set out should be established, composed of one member of the Department of Munitions and Supply, one member of the Income Tax Division and one member to be selected from outside the Government Service to act as Chairman of the Board;

Therefore the deputy of His Excellency the Governor General in Council, on the recommendation of the Minister of National Revenue and under the authority of the War Measures Act, Chapter 206 of the Revised Statutes of Canada 1927, and having regard to the provisions of the Income War Tax Act and the Excess Profits Tax Act, is pleased to order that a Board, to be known as the "War Contracts Depreciation Board," composed of

The Honourable Charles Patrick McTague, of the Supreme Court of Ontario, as Chairman;

Mr. Francis Henry Black, C.A., of the Department of Munitions and Supply; and

Mr. Robert Ferrier Burns, C.A., of the Income Tax Division;

be and it is hereby established.

The deputy of His Excellency the Governor General in Council, on the same recommendation, is hereby further pleased to order that the powers and duties of the said Board, or other successors appointed by the Governor in Council, and the regulations under which the Board shall act, shall be as follows:

1. To determine if the contract is a "War Contract" as defined in the initial Regulations hereunder;

2. To determine that the capital expenditures incurred were in connection with the fulfilment of the terms of the said "War Contract" and necessarily incidental thereto;

3. To determine the amount of the capital expenditures made;

4. To issue a certificate, substantially in accordance with the form hereto attached, based on the evidence secured and referred to therein;

5. To determine what part, if any, of the said capital disbursements have no reasonable post-war value, and thereby to determine the amount of such capital expenditures upon which special depreciation may be allowed;

6. To determine in any case or cases which they think advisable the annual rate or other rate of depreciation to be used in respect of any capital expenditure incurred under a War Contract, and in the absence of such determination by the Board, the Minister of National Revenue shall set the rate of depreciation.

7. To require contractors holding War Contracts to supply such evidence as may be required by the Board to make the determinations necessary for the issuing of a Certificate, substantially in accordance with the form hereto attached, to the Minister of National Revenue, certifying as to the facts upon and in respect of which special depreciation may be given.

8. To issue such Regulations from time to time hereafter, with the approval of the Minister of National Rev-

enue, as may be necessary to carry out the purpose and intent of this Order in Council.

Initial Regulations

1. (a) A "War Contract" shall be deemed to include any contract with the Dominion Government, the British Government or the Government of any of the Allies or their authorized agents, entered into for the purpose of securing war supplies of any nature from contractors who are required to expend capital sums in the construction or purchase of capital assets constructed or acquired after September 9, 1939, for the purpose of fulfilling any such contract, provided the assets are subject to depreciation by way of use in effecting fabrication and delivery of the said supplies.

(b) A contract entered into as a sub-contract under the above described contracts, or in furtherance thereof, which requires the construction or purchase of capital assets within the terms of the above, shall be deemed to be within the meaning of the term "War Contract."

(c) The term "War Contract" shall also extend to contracts entered into between subject and subject contracting for war purposes and constructing or purchasing capital assets which are subject to depreciation and which can be certified to by the Board as in the Regulations referred to, as being wholly necessary for the carrying out of war contract work, and that such capital assets will not have any reasonable post-war value to the contractor.

(d) The term "War Contract" shall not include any contract entered into prior to the 9th September, 1939, unless the Board and the Minister of National Revenue are satisfied that in all other respects except as to date, the contract is within the terms set forth above.

2. A certificate of *special depreciation may be*

(a) given to any company in respect of the cost of self-paid-for capital depreciable assets acquired for the production of war materials, excluding assets having a reasonably full post-war use;

(b) confined to war-time construction or assets acquired specifically for war purposes.

3. A certificate may issue when the terms of the War

Contract provide specifically that depreciation is to be secured through the medium of the unit purchase price.

4. A certificate may issue when the War Contract is silent as to the terms of depreciation.

5. A certificate of *special depreciation should not be*

(a) given when the contractor recovers the cost of capital assets separately and directly as such

(i) in a lump sum;

(ii) by instalments;

(iii) on engineer's progress reports.

(b) given if the capital assets are paid for by the Government under any "cessation of hostilities" clause contained in the contract. The Board shall certify in all such cases the character or nature of the payments made and the extent thereof. If a certificate has already been issued, it should be cancelled.

6. Sub-contractors under principal War Contracts may be dealt with in exactly the same manner as principal contractors holding War Contracts and special depreciation will only be allowed if sub-contractors produce evidence satisfactory to the Board and upon which the Board might issue a certificate to the Minister of National Revenue.

7. In all cases the certificate of the Board shall be without force or effect if the Minister of National Revenue finds that the contractor has failed hereafter to—

(a) keep separate accounts in respect of the particular capital assets concerned;

(b) maintain the identity of the physical capital assets in his financial records.

8. Special depreciation granted under any certificate shall be in lieu of normal depreciation usually allowed.

The deputy of His Excellency in Council is hereby further pleased to direct that the Board shall be supplied with a secretary and such additional clerical help as may be required, the appointments to be made to the Income Tax Division and seconded to the Board for service.

A. D. P. HEENEY,
Clerk of the Privy Council.

DOMINION OF CANADA

War Contracts

Certificate on which to base Special Depreciation

To the Minister of National Revenue,
Department of National Revenue.

Inasmuch as Section 6 of the Income War Tax Act provides that the Minister in his discretion may allow extra depreciation in the case of plant and equipment built or acquired to fulfil war orders for war purposes, this is to certify that—

1. A War Contract was made

Between

....
(Government Body concerned)
and

....
(Contractor)

....
(Sub-contractor)

The ..... contract is dated the ..... day of ..... 1940.

2. Capital assets of a depreciable character were constructed or acquired entirely at the expense of the ...... contractor and

(a) They were necessary for the performance of the said War Contract;

(b) They were not purchased or constructed prior to the commencement of the present war;

(c) It is believed that they will not have a reasonably full post-war business value;

(d) They were erected, installed or purchased to fulfil the terms of the War Contract after the commencement of the present war and have been used therefor to the date hereof;

(e) They cost in cash $...... of which special depreciation is to be allowed on $...... thereof.

(f) The respective group-costs and general description by classes or categories of the capital assets paid for and used in fulfilling the terms of the......contract have been verified by an affidavit of a duly authorized officer of the ...... contractor.

3. The terms of the said War Contract—

(a) provide specifically for reimbursement of depreciation through the medium of the unit purchase price for the war materials;

(b) are silent as to depreciation being reimbursed through the unit purchase price paid for the war materials;

(c) provide for payment of the said capital assets as such, apart from the unit purchase price paid for the war materials.

(Inapplicable paragraphs to be struck out and initialled.)

(Identify (a), (b) or (c) with essential terms of the contract by explanation.)

4. No reimbursement of capital expenditures incurred has been or is to be made, other than through the medium described in Item 3 ( ) above.

5. The annual rate of depreciation shall be ......% of item 2(e).

Dated at Ottawa, this ...... day of ...... 1940.

....
(Government body concerned)

....

This is the ...... Certificate issued in respect of the above .... contractor.

—— : : ——

Editor's Note: Since the publication in *The Canada Gazette* of the above regulations of the Board and form of certificate, we have received inquiries about the procedure to be followed by the contractor in applying for special consideration in respect of depreciation. We in turn have inquired of Mr. Justice McTague if there is a special form of application to be filled in and submitted by the contractor to the War Contracts Depreciation Board. His Secretary has replied as follows:

WAR CONTRACTS DEPRECIATION BOARD

385 Wellington Street,
Ottawa, Ontario,
19th September 1940.

A. H. Carr, Esq., C.A.,
Secretary-Treasurer,
The Dominion Association of Chartered Accountants,
10 Adelaide Street East,
Toronto, Canada.

Dear Sir:

Receipt of your letter of September 17th is acknowledged.

There is no special form of application to be filed by the Con-

tractor. Claims will usually be submitted in the first instance by letter from the Contractor and will then be developed by correspondence until all relevant information has been received. The date for hearing before the Board will then be set and the matter settled by discussion. The hearings before the Board will be held at Ottawa, unless sufficient volume of claims comes from any one district, to warrant the Board travelling to that district.

In the first letter to the Board, the following general information should be given:

1. A copy of the Contract which occasioned the Capital Expenditure against which special depreciation is claimed;

2. A complete statement of the Capital Expenditure incurred, verified by affidavit of the Contractor;

3. A submission stating the reasons for claiming special depreciation, giving the annual rate of depreciation deemed adequate and the Contractor's estimate of the post-war value of the project.

The form of Certificate, as published in the *Gazette*, was merely a draft form and the final form of the Certificate has not yet been decided on.

As soon as the final form of Certificate is prepared, a copy of the same will be forwarded to you. If there is any change in the regulations, as published in the Gazette, or in the procedure as outlined above, you will be advised in due course.

Yours faithfully,

WAR CONTRACTS DEPRECIATION BOARD

TNK:MM

(signed) T. N. Kirby
Secretary.

INDUSTRY IN SASKATCHEWAN

Saskatchewan has long been regarded by many as a province whose economy depends almost entirely upon agriculture. While it is true that the province is predominantly an agricultural area, secondary industries have recently been assuming a proportionately larger share in the value of Saskatchewan's productivity, and there are wealthy potential resources for further industrial expansion.

Industrial Canada, the official publication of the Canadian Manufacturers' Association, in its June 1940 issue carried an article by E. R. Kennedy, assistant secretary of the prairie division of the Association, on "Industrial Development and Possibilities of Saskatchewan." For many years, Mr. Kennedy points out, Saskatchewan has ranked last on a per capita basis among the provinces in the value of its manufactures but there are strong indications that the province will soon be making rapid industrial progress with manufacturing assuming still greater importance in the provincial economy. In its infancy Saskatchewan was settled by a farming population attracted solely by the fertility of the soil. It became a producer of wheat for which there was then an expanding and profitable market, and a market for, not a producer of, manufactured goods. Industrial production was slowly developed, however, and in 1939 Saskatchewan produced goods valued at about $70 millions, had a payroll of more than $7.2 millions and a capital investment of $42 millions. The record is creditable in view of the brief history of the province which was created only in 1905.

Saskatchewan's major industries, flour milling, meat packing and creameries, are closely allied to its agriculture. These three industries, with gross annual outputs respectively of $20 millions, $10 millions and $8 millions, account for slightly more than half of the annual gross value of manufactured products. The remainder of the annual industrial output is diversified over a wide range of concerns such as aerated water plants, bakeries, breweries, printing establishments, sawmills and woodworking factories. A clay plant in the southern part of the province is producing fire bricks and other refractory shapes used by the railways and industries of Canada. Several plants are produ-

cing sodium sulphate for the export market. General Motors of Canada operates a car and truck manufacturing plant at Regina. In the Bienfait area there are practically inexhaustible deposits of lignite, and about one million tons of coal are produced there annually and marketed throughout the prairie provinces. Deep seam mining operations are giving way to the more economical stripping method under which a larger tonnage is to be expected. After a long series of experiments a commercial briquette has been developed and is being successfully marketed. Hard rock mining is also assuming a place in the industrial development of the province, and the first gold brick was recently poured at the Gold Fields mine of Consolidated Mining and Smelting Company. The Pre-Cambrian shield cuts across the northern half of Saskatchewan and is considered to be as potentially rich in mineral resources there as it is farther east. Near Lloydminster on the western boundary a rich oil field has been brought into production with several gas and crude oil wells in operation, and exploratory work is being conducted in other prospective oil fields.

The province is well endowed with natural resources in the form of large deposits of mineral salts, volcanic ash and clays capable of being worked into products varying from common brick and tile to pottery and fine china. It is interesting to note in this respect that Mr. M. W. Kynch, in an article in the October 1937 issue of THE CANADIAN CHARTERED ACCOUNTANT stated: "Some of the clays already tested have been pronounced equal to any used for the finest pottery and china in any part of the world. A fine quality of bentonite or bleaching clay, used extensively in various leading industries, is present in southern Saskatchewan in quantities which an outstanding French engineer estimates to be sufficient to supply the needs of the world for many years to come. . . . Practically none of this valuable mineral has been commercially exported from Saskatchewan despite the ready European market yearning for supplies."

A growing realization on the part of the people of Saskatchewan that the future prosperity of the province depends on a more diversified economy is an encouraging sign that these vast resources of the province will not be allowed to lie dormant for want of exploitation.

AN ENGLISH INCOME TAX CASE

The Accountant Tax Supplement of 18th May 1940 reports the decision of the House of Lords in an interesting income tax case, *Lowry (Inspector of Taxes)* v. *Consolidated African Selection Trust, Ltd.*

The case, which centres around the issuance of shares to employees of the company at less than market value, reflects legal principles which might be applied in Canada under similar circumstances, although the reader will understand that the income taxing statutes of this country and Great Britain are not parallel. The facts of the case and the decisions of the Courts are as follows:

In 1933 the company passed a resolution to increase its capital and to provide that 10,000 of the new shares be reserved for issue to the employees at such time and on such terms as the directors should determine. In June 1934, when the shares were salable on the market at between £2 and £2 5s. per share, the company offered a block of 6,000 shares to certain employees at their par value of five shillings per share. The employees accepted the shares and were assessed to tax on the sums representing the difference between the par and the market value of the shares respectively allotted to them as being part of their earnings in the service of the company. The company was assessed to income tax for the year 1936-37 without any deduction being made from its profits in respect of the shares so allotted.

The company appealed the assessment contending that the amount of the difference mentioned above should be admitted as a deduction in computing its profits on the ground that if the shares had been sold at their market value the premium realized could have been paid to the employees as part of their remuneration. In that case the right to deduct the amount from profits could not have been questioned. The Crown contended that no expense had been incurred or, alternatively, that if any expense had been incurred it was chargeable to capital and not to revenue.

The General Commissioners of Taxation upheld the contention of the company but, on an appeal by the Crown, the King's Bench Division of the High Court reversed their

decision and held that "there was no justification for treating as an expense the premium which the company might have but did not in fact obtain." The company then appealed this decision and was sustained in the Court of Appeal which, allowing the appeal with costs, held that "the company had by way of remuneration paid its employees in money's worth, and that it was entitled to the deduction claimed." The Crown finally carried the case to the House of Lords which (in a majority decision given 8th May 1940, two out of five dissenting) reversed the decision of the Appeal Court and, sustaining that of the High Court, held that "the issue of the shares in the manner adopted did not involve expenditure 'wholly and exclusively laid out for the purposes of the trade' and it was not entitled to the deduction."

CONSOLIDATION OF INCOME WAR TAX ACT

A consolidation of the *Income War Tax Act* including all amendments of the 1940 session of Parliament may be obtained on written application to the King's Printer, Parliament Buildings, Ottawa, at a cost of twenty-five cents.

PAMPHLET ON NATIONAL DEFENCE TAX

The Department of National Revenue, Income Tax Division, has prepared a useful booklet concerning the application of the National Defence Tax, being section 91 of the *Income War Tax Act*. (See pages 189-192 of the September 1940 issue of THE CANADIAN CHARTERED ACCOUNTANT). The booklet also contains the administrative rulings issued in connection with this tax.

In a letter which we have received from Mr. C. Fraser Elliott, Commissioner of Income Tax, Ottawa, it is stated that copies of the pamphlet have already been distributed to every company in Canada, to trust companies and to a wide list of addresses, many of whom are accountants.

Any of our readers who have not received a copy of this free booklet may apply for one to the nearest Inspector of Income Tax who, we are assured, will send it by return post.

THE DOMINION ASSOCIATION OF CHARTERED ACCOUNTANTS

OFFICERS AND COUNCIL

Executive Committee 1940-41

President	W. G. Rowe, C.A., Vancouver, B.C.
Vice-Presidents	Frederick Johnson, C.A., Winnipeg, Man. T. Harold Johnson, C.A., Halifax, Nova Scotia
Immediate Past President	Kenneth W. Dalglish, C.A., Montreal, Que.
Chairman, Finance Committee	Kris A. Mapp, F.C.A., Toronto, Ontario
Chairman, Legislation Committee	Henry G. Norman, C.A., Montreal, Que.
Additional Member Executive Committee	Malcolm C. McCannel, C.A., Edmonton, Alberta
Secretary-Treasurer	Austin H. Carr, M.A., C.A., 10 Adelaide St. East, Toronto

Council 1940-41

Representatives	*Elected by*
H. A. Black, C.A., Edmonton M. C. McCannel, C.A., Edmonton J. H. Williams, F.C.A., Calgary	The Institute of Chartered Accountants of Alberta
W. G. Rowe, C.A., Vancouver R. W. Underhill, C.A., Vancouver J. Haydn Young, C.A., Vancouver	The Institute of Chartered Accountants of British Columbia
William Gray, C.A., Winnipeg Alexander Gray, C.A., Winnipeg Frederick Johnson, C.A., Winnipeg	The Institute of Chartered Accountants of Manitoba
Arthur E. Cox, F.C.A., Saint John H. L. McMackin, C.A., Saint John	The New Brunswick Institute of Chartered Accountants
H. J. Egan, C.A., Halifax J. E. Lloyd, C.A., Halifax	The Institute of Chartered Accountants of Nova Scotia
J. F. Gibson, F.C.A., Toronto F. C. Hurst, F.C.A., Toronto W. G. H. Jephcott, F.C.A., Toronto	The Institute of Chartered Accountants of Ontario
D. F. Archibald, C.A., Charlottetown T. H. Johnson, C.A., Halifax	The Institute of Chartered Accountants of Prince Edward Island
Wm. H. Campbell, C.A., Montreal H. G. Norman, C.A., Montreal Alfred Smibert, C.A., Montreal	The Society of Chartered Accountants of the Province of Quebec
C. P. DeRoche, C.A., Saskatoon M. Hesford, C.A., Swift Current G. G. Patrick, C.A., Saskatoon	The Institute of Chartered Accountants of Saskatchewan

Chairman, Committee on Education and Examinations—Gerald Jephcott, F.C.A.
Chairman, Committee on Accounting Terminology—John Parton, F.C.A.
Committee on Research—D. McK. McClelland, F.C.A.

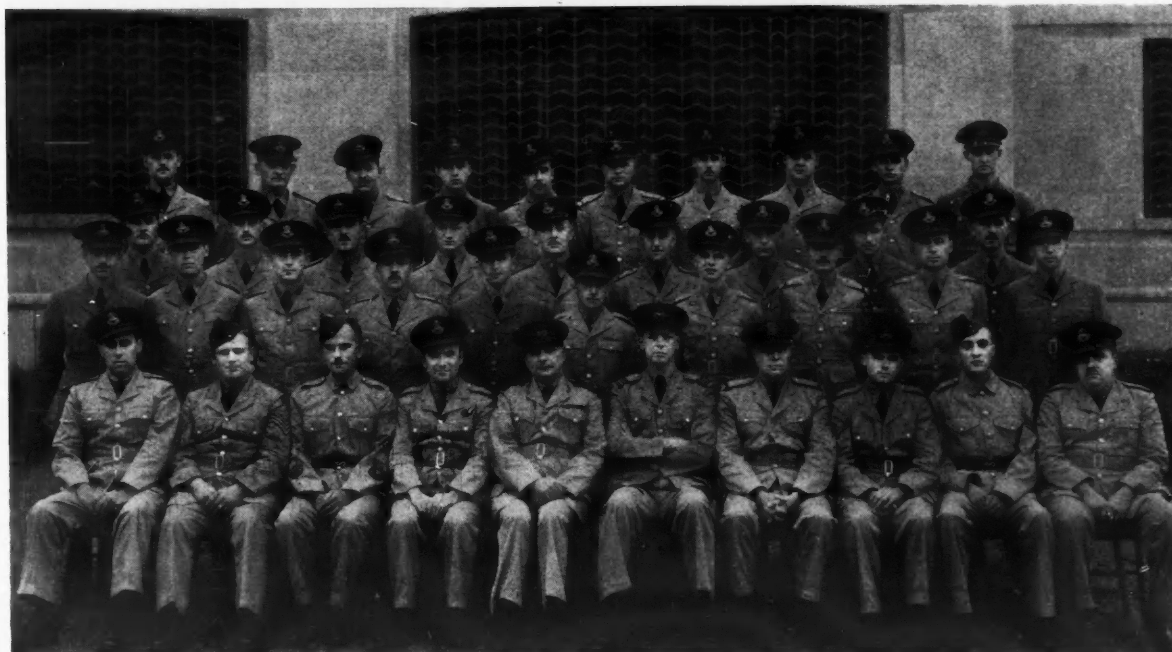
The Dominion Association of Chartered Accountants

President

W. G. ROWE, C.A.
Vancouver, B.C.

At the annual meeting held in Montreal, Quebec, September 5th, Mr. Rowe was elected President of The Dominion Association of Chartered Accountants for the year 1940-41.

No. 1—Accountant Officers' Course, St. Thomas, Ontario, July 1940 (see page iv)



No. 2—Accountant Officers' Course, St. Thomas, Ontario, August 1940 (see page iv)

No. 1. ACCOUNTANT OFFICERS' COURSE JULY 1940

(Photograph page ii)

Front row: F/Sgt. J. B. Teaffe, Cpl. D. S. Sisk, W/O. J. W. Robertson, F/O. J. J. E. Canty, W/C. F. C. Chalmers (RAF), F/O. G. A. P. Brickenden, S/Sgt. W. A. Hicking, Sgt. G. C. Hodgins, F/Sgt. J. R. Gray.

Second row: Pilot Officers A. W. Stempel, J. A. Baldwin, J. H. Broughton, R. E. Waller, L. P. Kent, E. H. Sharpe, M. S. Sutherland, K. M. Place, K. J. Dadson.

Third row: Pilot Officers J. M. Wynn, H. W. Sutherland, H. L. Good, W. A. Hobson, G. A. Cruickshank, D. C. J. O'Brien, G. L. McIntosh, J. Kergan.

Fourth row: Pilot Officers E. L. Gerow, T. A. Derrick J. P. Redpath, J. H. K. Broughton, J. LeM. Carter, J. T. Watt, H. D. F. Filleul, J. W. Bootle, W. G. Rathie, J. G. Vickery, G. L. MacKinnon, J. C. Byers.

No. 2. ACCOUNTANT OFFICERS' COURSE AUGUST 1940

(Photograph page iii)

Front row: P/O. G. A. MacDougall;
Staff: Sgt. G. C. Hodgins, W/O. J. W. Robertson (RCAPC), F/O. E. H. Andrew, F/Lt. J. S. Eley (RAF), S/Ldr. D. F. Syder (RAF) Officer Commanding, F/O. G. A. Brickenden, F/O J. J. Canty, S/Sgt. W. A. Hickling (RCAPC);
P/O. H. M. Cootes.

Second row: Pilot Officers C. H. Cowperthwaite, D. F. Archibald, C. C. Stewart, R. R. Beaudin, R. M. Cockburn, H. H. Gawthorp, B. M. Sears, S. B. Rhude, D. G. White, R. W. Hopkins.

Third row: Pilot Officers G. M. Monteith, C. E. Bazett, G. E. Wilson, B. M. Adair, J. S. Owen, J. A. Hall, J. R. Jackson, J. H. Insley, J. E. Black.

Rear row: Pilot Officers J. F. Broadhead, E. D. Martin, R. H. Gregson, G. M. Steele, F. P. Blackmore, L. E. Fingarson, W. G. Davison, F. L. Lauer, A. R. Bevan, J. M. Lavery.

GENERAL NOTES

Report of Annual Meeting

The thirty-eighth annual meeting of The Dominion Association of Chartered Accountants was held in the Mount Royal Hotel, Montreal, on Thursday 5th September. The Executive Committee met on Monday evening the 2nd, and the Council all day Tuesday, Wednesday morning and at the close of the annual meeting on Thursday afternoon. Kenneth W. Dalglish, C.A., Montreal, President of the Association, presided at the sessions. The Committee on Education and Examinations met on Wednesday afternoon under the chairmanship of Kris A. Mapp, F.C.A., Toronto.

On account of our country being occupied with the war effort, the annual meeting of our Association this year was confined to one business session, without the usual round-table conferences on accounting subjects and the presentation of technical papers. The attendance was in consequence reduced, a total of only seventy members being present. All nine Provincial Institutes were represented as follows: Alberta four, British Columbia three, Manitoba three, New Brunswick one, Nova Scotia three, Ontario seven, Prince Edward Island one, Quebec forty-three and Saskatchewan five.

Membership—The annual reports to this year's meeting by the nine Provincial Institutes showed that good progress had been made during the previous year. The membership of the Institutes at 31st May last was 2422 which is an increase of 95 members over that of a year ago. Of this total, 1434 or 60 per cent are in the practice of the profession. An examination of the membership lists of the Institutes shows that 124 memberships are duplicated, which means that the individual members of the profession number 2298.

Education and Examinations—The councils of the Institutes continued to give considerable time and thought during the past year to providing educational facilities to their students. Six Institutes are using the instruction course of the Ontario Institute and another Institute recommended that its students take this five-year course of study. Two other Institutes have closely co-operated with local universities in the holding of classes and most of the

Institutes have added to the facilities of their reference libraries. It was noted that the Student Associations in some of the Institutes were active during the past year in arranging series of lectures and study groups and that they had received the ready co-operation of the members of their respective Institutes.

During the year uniform examinations of the Provincial Institutes were put into operation for the first time, and the reports of the several Institutes expressed satisfaction over the results of this new plan whereby all the prospective members of the profession will be writing the same examinations.

Reports of Committees—A more detailed report of the meeting will be published in the 1940-41 Year Book of the Association. Reports of excellent progress were presented by other committees of the Association, namely those on legislation, finances of the Association, "The Canadian Chartered Accountant," accounting terminology, accounting research (which had devoted its attention particularly to the "Extensions of Auditing Procedure"), public relations, and by-laws.

Entertainment—The customary program of entertainment was absent from this year's meeting. In previous years the Institute in whose province the annual meeting is held has provided the entertainment for the convention. The action of the Quebec Society of donating to the Dominion Government for the national war effort the customary amount spent on entertainment was heartily approved by the meeting.

Officers—The following are officers of the Association for the year 1940-41: President, W. G. Rowe, C.A., Vancouver; vice-presidents, F. Johnson, C.A., Winnipeg, and T. H. Johnson, C.A., Halifax; immediate past president, Kenneth W. Dalglish, C.A., Montreal; chairman of finance committee, Kris A. Mapp, F.C.A., Toronto; chairman of legislation committee, H. G. Norman, C.A., Montreal; additional member of executive committee, M. C. McCannel, C.A., Edmonton; secretary-treasurer, Austin H. Carr, M.A., C.A., Toronto.

Our Contributors This Month

PHILIP THOMPSON CLARK who writes on corporation taxes in Ontario is a member of the Institute of Chartered Accounts of Ontario (1930). Before becoming assistant Controller of Revenue for the Province of Ontario in 1936 and being placed in charge of the administration of the Corporations Tax Act of that Province, he had acted for three and a half years as an assessor of corporation income tax at Toronto with the Income Tax Division of the Department of National Revenue.

In the year 1934-35 a series of five articles on grain accounting prepared by members of the Manitoba Institute was published in THE CANADIAN CHARTERED ACCOUNTANT. A brief reference therein was made to The Lake Shippers' Clearance Association, which is the subject of the instructive article by William H. Gray published this month. Mr. Gray attended the University of Manitoba (Arts Course) for two years, 1933 to 1935, was employed by Messrs. George A. Touche & Co., chartered accountants, Winnipeg, for the next three years and passed the intermediate examination of the Institute of Chartered Accountants of Manitoba in 1938. He attended Queen's University, Kingston, for the next two years, where he had a fine record as a student and graduated in May 1940 with the degree of B.Com. He is now continuing his studies to qualify as a chartered accountant.

Congratulations to Fred Johnson's Son

The many friends of Frederick Johnson, C.A., Winnipeg, who has taken so great an interest in the education of students for our profession, will be gratified to learn that his son Allen has this year won the provincial scholarship for Manitoba offered annually by Queen's University, Kingston, to the student standing highest on his or her entrance standing from each province of Canada. The scholarship, which is a substantial one, consists of $100 in cash and free tuition for each of three years at the University.

December Examinations

The timetable of the December 1940 uniform examinations in the Intermediate and Final grades was announced

by the Board of Examiners-in-Chief in our September issue (page 204).

The dates of writing any other examinations, including those for the Primary grade, and for law, economics, etc., will be arranged for its own candidates by each Institute.

Export Credit

In our September issue was published the very instructive article by F. Bradshaw Makin on the functioning of the British Export Credits Guarantee Department. Mr. Makin in his letter of 19th August writes: "Since the article was written a further addition has been made to the cover issued by the Department. The latest development is the issue of a C. I. F. policy, which allows an exporter to insure himself for six months ahead against the risk of any rise in marine insurance, freight rates, war risk insurance, and so enable him to quote a firm price some months prior to delivery. This new policy is additional to the recent pre-shipment policy which covered the exporter against 90% of the loss risk if, for reasons beyond his control, he is unable to deliver the goods actually ordered. A single policy covering solvency 85%, transfer 90% and pre-shipment 90% is now available to exporters."

The Royal Canadian Air Force

In this issue we reproduce the photographs of the class taking the Accounting Officers' Course in July 1940 and in August 1940 held at St. Thomas, Ontario.

In a letter dated 5th July 1940, Wing Commander K. G. Nairn, Director of Accounts for the R. C. A. F., conveyed his appreciation of the response to his request for members of the profession in Canada to assume commissions in the R. C. A. F. in connection with the Pay and Accounting Services. "Thirty Officers, representing entries from the Institutes in each of the Provinces," he stated, "are at present undergoing initial training at St. Thomas. From there they will be attached to the various Commands and Operational Stations. A like number will be following along for the August course. The work that they will be doing will be of considerable responsibility, and it is felt that they will be giving valuable service to the Royal Canadian Air Force."

OBITUARY

The Late F. P. Page

The Institute of Chartered Accountants of British Columbia announces with regret the death at Ipswich, England, on 11th July last of F. P. Page, an honorary Fellow of the Institute. Mr. Page who was admitted a member of the Institute in 1911 had resided in England for many years before his death.

BOOK REVIEW

STATISTICAL METHODS AS APPLIED TO ACCOUNTING REPORTS

By A. A. Fitzgerald

(Published by *Accountants Publishing Company, Limited,* Melbourne, Australia, 1940, paper, 96 pages, 3/6)

The increasing reliance of modern business upon statistics, both internal and external, in the planning, conduct and control of operations has rendered the possession of some knowledge of statistical techniques by professional accountants a necessity, particularly those engaged in consulting work.

A recognition of this fact has led to the publication of this admirable little work written by the President of the Commonwealth Institute of Accountants of Australia. Although designed primarily for students of the Institute in that Dominion it still has much to commend it to the practising accountant.

Inasmuch as the volume is intended as an introductory text the author has not attempted to retrace all the ground covered by the standard reference works in the subject. Rather, in lucid but terse language, Mr. Fitzgerald has confined himself to the more salient aspects of the subject and always with the requirements and point of view of the accountant in mind.

The questions of the collection and tabulation of statistical data, graphics, dispersion and time series are discussed briefly but understandingly. Numerous practical illustrations have been included to lend force and interest to the subject treatment.

It is rather regrettable that the limitations of space did not permit a slightly more comprehensive examination of the mechanical tabulating and accounting equipment so widely used today. In addition, the mathematical methods outlined for the analysis of time series, particularly long-term trend, are given an air of finality which most business statisticians would be unwilling to concede to them. It must be admitted, however, that the author has performed very ably the task he assigned himself.

R. B. Willis.

Department of Business Administration,
University of Western Ontario,
London, 3rd September 1940.

STUDENTS' DEPARTMENT

R. G. H. SMAILS, C.A., Editor

Notes and Comment

A year ago we wrote in these notes: "Those for whom it may be decreed that they can best serve the national emergency by pursuit of their civil occupations will have to combat a restlessness and impatience which otherwise would impair their powers of concentration and, hence, their effectiveness. Those to whom a more stirring and perhaps dangerous part is assigned will be kept in mind by the others who continue to turn the pages of the Students' Department." Although twelve months of tragic history have been unfolded since then, the words seem still to be appropriate, as the days shorten and another fall term opens in intensive preparation for the December examinations. But the restlessness to be combatted has become more acute; the "dangerous part" is being played in gallant earnestness.

* * *

The recommendation of the Royal Commission on Dominion-Provincial Relations that the provinces and their municipalities should withdraw entirely from the personal income tax field is based on the belief of the Commission that "the income tax should be used in accordance with modern practice, as the equalizer and chief instrument of adjustment in the whole tax system."[1] The Commission points out further that "If Dominion unemployment insurance and relief . . . should be put on a contributory basis, it is essential that the premiums be co-ordinated with the general income tax and the whole tax system."

This recommendation may be regarded as one of the most drastic proposals contained in the Report and it is likely to be vigorously challenged by those provincial authorities who regard an income tax as a source of prestige whose loss will not be balanced by award of a National Adjustment Grant. The average citizen, however, being more concerned in these days with the tremendous tax burden which falls upon him than with considerations of

[1]Report, Book II, p. 112.

administrative prestige, may be expected to support the recommendation with enthusiasm.

The Report as a whole (and particularly its proposals for the re-allocation of financial jurisdiction) has become a matter of greater rather than less urgency as a result of the war. The fiscal needs of the Dominion Government for years to come will be enormous and there will shortly be in operation a contributory unemployment scheme of the type which renders adjustment of the personal income tax absolutely essential.

* * *

STUDENTS' ASSOCIATION NOTES

BRITISH COLUMBIA

The annual field day and dinner meeting of the Students' Society of the Institute of Chartered Accountants of British Columbia took place on September 6th.

The afternoon was devoted to tennis and golf matches and a large turnout provided plenty of competition. The Gyles-Foster Golf Cup was carried off by F. H. Field, while the Tennis Cup, donated by Messrs. Haydn-Young and Buttar, was won by R. D. Young.

Following the tournaments the annual dinner meeting was held at the Pacific Athletic Field. After the presentation of prizes a lively discussion took place on the problems confronting the members.

Members elected to the Council for the ensuing year were: Messrs. A. H. Affleck, J. T. Biller, D. G. Dunbar, J. Frazee, W. T. Powers, F. E. Walden and R. D. Young.

* * *

PROBLEMS AND SOLUTIONS

Solutions presented in this section are prepared by practising members of the several provincial Institutes and represent the personal views and opinions of those members. They are designed not as models for submission to the examiner, but rather as such discussion and explanation of the problem as will make its study of benefit to the student.. Discussion of solutions presented is cordially invited.

PROBLEM I.

THE PROVINCIAL INSTITUTES OF
CHARTERED ACCOUNTANTS
FINAL EXAMINATION, 1939
AUDITING II

Question 6

The Great Neck Falls Power Co., Ltd., a Dominion Company, has outstanding a 6% First Mortgage Bond Issue of $1,500,000.00; 6%

Preferred Stock of $500,000.00, and 50,000 n.p.v. common shares. It has also borrowed considerable sums of money from the bank.

Under a plan to reduce fixed charges, and provide ample working capital, arrangements have been made whereby a firm of investment bankers will underwrite an issue of $2,000,000 4% First Mortgage and Refunding Bonds, and 20,000 shares of n.p.v. common stock, the cash to be used for the purpose of:

(a) Retiring the existing bonds;
(b) Paying off the bank loan;
(c) Defraying the expenses of underwriting, etc.,
(d) General purposes of the Company.

The Underwriters will make a public offering of the securities, at a price of $120.00 per unit of one $100.00 bond and one share of n.p.v. common stock.

Employed to make an investigation for the purpose of supplying a certificate of profits for the prospectus, you have verified the following figures for the past four years:

	Year ending 30th June			
	1936	1937	1938	1939
Operating Profit, before depreciation, interest, and income tax	$450,000	$426,000	$445,000	$465,000
Allowance for depreciation......	175,000	173,000	172,000	176,000
Interest on bonds and loans.....	112,000	114,000	116,000	118,000
Profit on Sale of Investments...		22,000		
Loss on Scrapped Machinery.....			18,000	

Dominion and Provincial Income Taxes may be taken as aggregating 17%

REQUIRED: The certificate of profits which you would sign for insertion in the prospectus.

DISCUSSION AND SOLUTION

When an accountant is employed to conduct an investigation leading to a certificate of profits for inclusion in a prospectus, the purpose is to obtain an expert opinion of the amount of normal profit, in the period covered by the investigation, which would have been available for the purpose of paying interest and/or dividends on the securities offered in the prospectus.

To arrive at the required figures, the accountant will usually find it necessary to make certain eliminations from, and adjustments to, the published figures, and, to be justified in making these changes, must satisfy himself that the required money from the sale of the securities will be actually available to the Company, and that it will be applied in a certain manner. His certificate will usually include a statement that satisfactory evidence covering these matters has been produced to him.

It should be noted that Section 77 (3) of *The* [Dominion] *Companies Act, 1934* requires that items of a non-recurring nature shall be shown separately.

Bearing the above requirements in mind, the candidate should proceed to determine the figures he requires for his certificate, and to draw the certificate, incorporating the figures therein. Although the wording of such certificates and the amount of detail shown vary considerably according to the personal opinion of the accountant and the particular circumstances, conciseness should be aimed at, provided that all pertinent information is given. It is perhaps unnecessary to add that the profits must be shown by individual years and not

merely as an average, and that the accountant should confine himself to facts and not indulge in predictions or observations on the merit or otherwise of the securities offered.

In the particular example under consideration, the securities to be offered are of two kinds, viz., bonds and common shares. It is important, therefore, to show:

(a) the amount which would have been available for payment of interest on the new bonds;

(b) the residue of profit which would have remained for dividends on the common shares.

Inasmuch as interest on bonds is a charge against profit before determination of income tax, the amount under (a) will be before computation of the tax; the amount under (b) will be after deduction of all charges and, in addition, provision for dividend on the senior stock issue.

The desired figures would be:

	Year ending 30th June			
	1936	1937	1938	1939
Operating profit	$450,000	$426,000	$445,000	$465,000
Depreciation	175,000	173,000	172,000	176,000
Amount available for interest on new bonds	275,000	253,000	273,000	289,000
Interest on new bonds	80,000	80,000	80,000	80,000
	195,000	173,000	193,000	209,000
Income taxes—17%	33,150	29,410	32,810	35,530
	161,850	143,590	160,190	173,470
Preferred dividend	30,000	30,000	30,000	30,000
Amount available for dividend on common	$131,850	$113,590	$130,190	$143,470

A suggested wording of the certificate follows:

The Great Neck Falls Power Co., Ltd.

Gentlemen—

I have made an examination of the books and accounts of your Company for the four years ended 30th June, 1939, and I have examined contracts and agreements covering the sale of $2,000,000 4% First Mortgage and Refunding Bonds and 20,000 shares of no par value common stock and the application of the proceeds of the sale.

I certify that, in my opinion, the profit of those years which would have been available for payment of interest on the new bond issue and dividends on the total common shares to be outstanding were as follows:

	Year ending 30th June			
	1936	1937	1938	1939
Profit available for bond interest	$275,000	$253,000	$273,000	$289,000
Interest on bonds (new issue)	80,000	80,000	80,000	80,000
Income taxes at current rates	33,150	29,410	32,810	35,530
Dividend on preferred stock	30,000	30,000	30,000	30,000
	143,150	139,410	142,810	145,530

Amount available for dividend on 70,000 common shares	$131,850	113,590	$130,190	$143,470

In arriving at the above figures, items which, in my opinion, are of a non-recurring nature, as follows, have been excluded:

	1936	1937	1938	1939
Interest on bonds and loans to be retired under present financing	$112,000	$114,000	$116,000	$118,000
Profit on sale of investments		22,000		
Loss on scrapped machinery			18,000	

Yours faithfully,

PROBLEM II.

THE PROVINCIAL INSTITUTES OF CHARTERED ACCOUNTANTS

FINAL EXAMINATION, 1939

AUDITING II

Question 7

As auditor of the X Company, Ltd., a public company incorporated under the Dominion Companies' Act, you are presented with the following Balance Sheet and Profit and Loss Account, made up by the Company's bookkeeper, for verification and certification:

BALANCE SHEET

As at 31st December 1938

ASSETS

Cash in bank and on hand		$ 32,786.00
Accounts receivable	$101,520.00	
Bills receivable	96,482.00	
	$198,002.00	
Less: Reserve for bad debts	10,000.00	
		188,002.00
Inventories		106,426.00
Prepaid insurance and taxes	1,314.00	
Bond discount	4,000.00	
		5,314.00
Land, buildings, plant, machinery and furniture and fixtures, *less* depreciation		312,245.00
Investments		147,822.00
Goodwill		50,000.00
		$842,595.00

LIABILITIES

Accounts payable	$ 48,248.00	
Accrued charges	1,618.00	
		$ 49,866.00
Bonds, 6%, due 1st January, 1949		150,000.00
Capital Stock:		
Preferred, 7% cumulative	50,000.00	
Common	375,000.00	
		425,000.00

Surplus:		
As at 1st January 1938	$213,480.00	
Profit for year ended 31st December, 1938	18,999.00	
	$232,479.00	
Less: Dividend paid	14,750.00	
		217,729.00
		$842,595.00

PROFIT AND LOSS ACCOUNT

For the Year Ended 31st December 1938

By Net Trading Profit, after all expenses of operation, including depreciation		$ 51,520.00
Income from investments		8,261.00
To Administrative expenses, including directors' fees	$ 24,600.00	
Depreciation of fixed assets not used in operations	686.00	
Bond interest	9,000.00	
Bond discount	1,000.00	
Bad debts	5,496.00	
Balance	18,999.00	
	$ 59,781.00	$ 59,781.00
By Balance—being Net Profit		$ 18,999.00

From your examination of the books, and explanations given to you, you discover the following facts:

1. The Company owns a controlling interest—90%—in another Company (also incorporated by Dominion Letters Patent) which it carries at the par value, $90,000. The stock was acquired at incorporation. The Subsidiary made a loss in 1938, which, with the dividend paid, was charged to its Surplus Account, which still shows a considerable balance at credit. The Holding Company credits dividends received to income, but does not otherwise deal with Subsidiary Company's profits or losses in its accounts.

2. Included in the accounts receivable are the following:

Amount due from subsidiary company	$26,342.00
Loan to director	1,500.00
Advances to shareholders	768.00

3. The Bills Receivable include $52,000 of the subsidiary company's notes.

4. Inventories were established by physical count. An analysis shows that they consist of:—Raw Materials, $18,240; Work-in-process, $28,716; Finished goods, $59,470. Owing to the difficulty of establishing the cost of raw materials, they have been valued at current market prices. Work-in-process and finished goods were priced at cost, but an all-round allowance of 10% was deducted as a conservative provision; cost is less than market price.

5. The Company was re-organized in 1929, and the fixed assets were appraised by the General Appraisal Co. on 15th January, 1930, the appraisal values being set up in the books on the re-organization of the Company. Subsequent additions have been capitalized at cost. The Depreciation Reserve is $134,275, and the total depreciation charge for 1938, at rates allowed by the Income Tax Department, was $13,218.

6. The authorized capital of the Company is $400,000 divided into shares of $100 each.

7. The investments, except for the stock of the Subsidiary, consist of marketable bonds and shares, the market value of which was $55,250 on 31st December, 1938.

8. The income from investments includes a dividend received from the Subsidiary of $1,800 and $2,650 dividends from Canadian companies.

9. No provision has been made for 1938 Income Tax, and this should be computed and allowed for. (Note: Ignore Provincial Income Tax.)

10. Salary and bonus of the Managing Director for 1938 was $8,500. The other Directors, who are not salaried employees, received total fees of $600.

11. The confirmation received from the bank indicated that the Company had $3,260 of Customers' paper under discount on 31st December, 1938.

Having regard to the requirements of *The* [Dominion] *Companies' Act, 1934* and amendments, draw up the accounts in proper form and attach your report.

DISCUSSION AND SOLUTION

Undoubtedly, in setting this question, the examiner's object was to test the candidate's ability to draw up statements conforming to accepted accounting practice and the definite requirements of Sections 112 and 113 of *The Companies' Act;* to write the Statutory Report and in addition, that special report required by Section 114 of the Act in cases where subsidiary companies' accounts are not consolidated with those of the Parent Company in its published accounts. A further, though probably less important, requirement of the question is the determination of liability for Dominion Income Tax.

A broad knowledge of the provisions of *The Companies Act,* and in particular of those sections affecting the work of the auditor, is an essential requirement for the accounting student, and it is suggested that the statements which follow be studied in conjunction with Sections 112 and 113 of the Act.

In drafting the Balance Sheet, assets and liabilities should, of course, be exhibited under suitable groupings and there is room for divergence of opinion as to the particular group in which certain items should be included. The examiner would no doubt have an open mind about this, irrespective of his personal predilection for a particular treatment. Thus, in the solution offered, marketable securities are included as a current asset at cost; some might prefer to include this asset under a separate heading as "Investments"; others again, might argue that if the item is included as a current asset it should not be stated at a figure in excess of realizable value. The difference between cost and market value was not very considerable in this instance, however, and, as market value is shown, many accountants would not consider it necessary to write down the item to market value even though included as a current asset. Similarly, some accountants would prefer to show "Prepaid Insurance and Taxes" as a non-current asset. Similar considerations affect the statement regarding valuation of inventories, the amount of the reserve might be shown. There is reluctance among directors to reveal this information, hence the amount of the reserve is not given in the solution offered; the important point is that the fact that there is a reserve be shown.

On the other hand, grouping of items might be definitely wrong, e.g., the inclusion of accounts and bills receivable owing by the Subsidiary under the heading of "Current Assets" (*vide* Section 112 (5) of the Act.)

A debatable point also arises in determination of income tax, in regard to the item "Depreciation of Fixed Assets not used in operations." If this represents depreciation of assets purchased for ordinary business operations, and unused because of lack of volume, it would probably be allowed as a deduction. If the assets were not purchased for the normal operations of the company, it would be disallowed.

Bond discount, which may bring the bond interest to the effective rate, is not allowed as a deduction in computing income tax owing to the limitation of the interest charge to the rate stated in the instrument creating the loan, in other words, the coupon rate.

Dividends received from other Canadian companies which are subject to tax, are exempt; and these include the dividend from the Subsidiary Company.

Probably the most difficult part of the question for the average candidate would be the wording of the report required by Section 114 of the Act, both because of the fact that these reports are required in comparatively few cases, and that the wording must vary in accordance with the particular circumstances. The somewhat involved language of the Section makes it difficult to determine the precise requirements in any particular case. A careful study of the Section indicates that, in this case, the report should contain:

(a) a general statement of how profits and losses of the subsidiary are dealt with in the parent company's books;

(b) in particular, how the loss sustained by the subsidiary in the period under review was dealt with; and

(c) the amount by which the profit shown would have been reduced had the parent company made provision for its share of the subsidiary's loss, and had it not included as income the dividend paid by the subsidiary out of accumulated profits of prior years.

It would seem to be immaterial whether the report required by Section 114 is included as part of the statutory report or separately.

The suggested solution follows:

THE X COMPANY, LIMITED

Balance Sheet as at 31st December 1938

ASSETS

Current:		
Cash on hand and on deposit		$ 32,786.00
Accounts receivable, trade	$ 72,910.00	
Bills receivable	44,482.00	
	117,392.00	
Less Reserve for bad debts	10,000.00	107,392.00
Loan to director		1,500.00
Advances to shareholders		768.00
Marketable securities (Market value $55,250)		57,822.00
Prepaid insurance and taxes		1,314.00

Inventories (established by physical count, and valued by the management as follows: Raw materials—at current market price; Work-in-process and finished goods — at cost which is less than market value, less Reserve.)	106,426.00	$308,008.00
CAPITAL STOCK OF, AND ADVANCES TO, SUBSIDIARY COMPANY		
Capital stock at par	90,000.00	
Account and bills receivable	78,342.00	168,342.00
DEFERRED CHARGE:		
Bond discount unamortized		4,000.00
FIXED:		
Land, buildings, plant, machinery and furniture and fixtures (at appraised values, as at 15th January 1930, as valued by the General Appraisal Co., with subsequent additions at cost)	446,520.00	
Less Reserve for depreciation	134,275.00	
	312,245.00	
Goodwill (at cost)	50,000.00	362,245.00
		$842,595.00

LIABILITIES

Current:		
Accounts payable	$ 48,248.00	
Accrued charges	1,618.00	
Provision for taxes	2,332.35	$ 52,198.35
BONDS—secured—6%, due 1st January 1949		150,000.00
CAPITAL STOCK:		
Authorized: 4,500 shares of $100 each	450,000.00	
Issued and paid-up:		
Preferred, 7% cumulative	50,000.00	
Common	375,000.00	425,000.00
SURPLUS:		
As at 1st January 1938	213,480.00	
Add Net profit for year ended 31st December 1938	16,666.65	
	230,146.65	
Less Dividends paid	14,750.00	215,396.65
		$842,595.00

CONTINGENT LIABILITY in respect of bills receivable discounted $3,260.

APPROVED ON BEHALF OF THE BOARD:

....)
) Directors
....)

THE X COMPANY, LIMITED

Profit and Loss Account for the Year Ended 31st December 1938

Net Trading Profit, after all expense of operation, including depreciation of fixed assets used in operation		$ 51,520.00
Administrative expenses	$ 15,500.00	
Remuneration of managing director	8,500.00	
Directors' fees	600.00	
Depreciation of fixed assets not used in operations	686.00	
Bad debts	5,496.00	30,782.00
		20,738.00
Income from investments		8,261.00
		28,999.00
Bond interest	9,000.00	
Bond discount amortized	1,000.00	10,000.00
		18,999.00
Provision for estimated income tax		2,332.35
NET PROFIT FOR THE YEAR		$ 16,666.65

NOTE: Depreciation charged to operating accounts	$ 12,532.00
Remuneration of legal advisers of the company	NIL

COMPUTATION OF INCOME TAX

Net Profit as shown	$ 18,999.00
Add Bond discount	1,000.00
	19,999.00
Less Dividends from Canadian companies	4,450.00
TAXABLE INCOME	15,549.00
Tax—15% of $15,549.00	$ 2,332.35

AUDITOR'S REPORT TO THE SHAREHOLDERS

PLACE AND DATE: I have audited the books and accounts of The X Company, Limited, for the year ended 31st December 1938, and I have obtained all the information and explanations I have required. In accordance with Section 114 of *The Companies Act, 1934*, I report that the profits of the Subsidiary Company are taken into the accounts of The X Company, Limited only to the extent of dividends received. The Subsidiary Company made a loss in the year ended 31st December

1938, which was charged to prior surplus in the books of the Subsidiary Company: no provision for its share of this loss was made in the books of The X Company, Limited. In my opinion, a provision of $ (amount undeterminable, as amount of loss not stated) would be necessary in the profit and loss account of The X Company, Limited, to fully provide for its share of the loss of the Subsidiary Company; and in addition, a dividend of $1,800.00 was received and treated as income by The X Company, Limited, which was paid out of prior years' surplus of the Subsidiary Company.

Subject to the foregoing, in my opinion, the above Balance Sheet and relative Profit and Loss Account are properly drawn up so as to exhibit a true and correct view of the state of the Company's affairs on 31st December, 1938, and the result of its operations for the year ended that date, according to the best of my information and the explanations given to me, and as shown by the books of the Company.

A. Practitioner,
Auditor.

TABLE OF EXCHANGE RATES

(Kindly supplied by The Canadian Bank of Commerce, Toronto)

	31st August 1940	*14th September 1940*
U.S. Dollars	10-11% P.	10-11% P.
Sterling	443-447	443-447
Australian Pounds	358½	358½
New Zealand Pounds	360	360
South African Pounds	446	446
Belgium—Belgas	No quote	No quote
Denmark—Kroner	No quote	No quote
Holland—Florins	No quote	No quote
Finland—Finmarks	221	221
France—Francs	No quote	No quote
Italy—Lire	No quote	No quote
Sweden—Kronor	2638	2637
Switzerland—Francs	2519	2518
Norway—Kroner	No quote	No quote

Note: The above quotations are expressed as follows: Pound currencies—Canadian cents per unit; Continental currencies—Canadian cents per 100 units.